

# FREQUENTLY ASKED QUESTIONS ABOUT COMMUNICATIONS ISSUES FOR ISSUERS AND FINANCIAL INTERMEDIARIES

These Frequently Asked Questions (FAQs) focus on the rules and regulations affecting communications. The Securities and Exchange Commission (the “SEC”) seeks to promote timely and robust disclosures by reporting issuers, while regulating communications made in proximity to, or about, proposed offerings of securities. Offering-related communications are subject to careful scrutiny in order to ensure that disclosures are fair and balanced and are not intended to condition the market for the offered securities. Over time, communications have become more dynamic, in large measure as a result of the proliferation of electronic means of disseminating information on a real-time basis. To address these developments, SEC regulations concerning communications have been made more flexible and contingent upon the type of company and its size and sophistication as we explain below.

These FAQs primarily address communications in the offering context (other than in the context of tender or exchange offers or business combinations) by issuers that are not investment companies, business development companies or other specialized issuers.<sup>1</sup>

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<sup>1</sup> Registered investment companies and business development companies are regulated under the Investment Company Act of 1940, as amended, and many of the rules discussed in these FAQs specifically exclude those entities from the benefits of

For additional information about the application of the federal securities laws to communications issues, *see*:

- **Use of Websites and Social Media by Issuers** – Frequently Asked Questions About Liability of Public Companies and Companies in Registration For Website and Social Media Content, available at <http://www.mofo.com/files/Uploads/Documents/FAQCompanyWebsiteContent.pdf>.
- **Disclosure by Reporting Issuers** – Frequently Asked Questions About Regulation FD, available at <http://media.mofo.com/files/Uploads/Images/FAQs-Regulation-FD.pdf>.
- **Research Analysts and Investment Banking** – Frequently Asked Questions About Separation of Research and Investment Banking, available at <http://www.mofo.com/files/Uploads/Images/Frequently-Asked-Questions-about-Separation-of-Research-and-Investment-Banking.pdf>.

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their safe harbors. These FAQs also do not address communications with shareholders. *See* our Guide to Social Media for more on these matters at <http://media.mofo.com/docs/pdf/170814-guide-to-social-media-and-the-securities-laws/>.

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## Communication Rules Overview

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### *What is an “offer” within the meaning of the federal securities laws, and why is it relevant to the communications rules?*

The term “offer” is defined broadly in Section 2(a)(3) of the Securities Act of 1933, as amended (the “Securities Act”), as “every attempt or offer to dispose of, or solicitation of an offer to buy . . . for value.” The Securities Act regulates all offers of securities unless there is an available exemption. Exemptions are available for private or limited offerings, offerings made outside the United States and offerings of certain exempt securities. A particular area of concern is offers that are made to the general public without the protections of the Securities Act. Therefore, the SEC regulates whether a particular communication is an “offer,” the manner in which communications are made, the contents of communications made in connection with offers of securities and who may make certain communications, including whether the person making the communication is an issuer subject to the reporting and other obligations (a “reporting issuer”) under the Securities Exchange Act of 1934, as amended (the “Exchange Act”).

### *What kinds of communications are not deemed “offers” or are protected by safe harbors?*

The SEC and the courts interpret the term “offer” broadly. The SEC has long cautioned that publicity prior to a proposed offering may be considered an effort to condition the market and create interest in the issuer or its securities in a manner that raises questions about

whether such publicity is part of a selling effort.<sup>2</sup> However, there are communications that do not constitute offers based on (i) the nature of the information in the communication, (ii) the timing of the communication, (iii) the purpose of the communication or (iv) the person making the communication. In most cases, common business communications are not “offers.”

The following is a brief outline of the primary safe harbors, which are discussed in greater detail in these FAQs. These safe harbors are non-exclusive, and other exemptions and protections may be available under applicable circumstances. It should also be noted that the exemptions and safe harbors do not protect actions that are in technical compliance with the applicable rule but have as their primary purpose conditioning the market or that are part of a scheme to evade the requirements of Section 5 of the Securities Act.

Issuers who are not subject to the reporting obligations of the Exchange Act (“non-reporting issuers”) may publish regularly released factual business information that is intended for use by persons other than in their capacity as investors or potential investors. (Rule 169)

Communications by issuers made more than 30 days before filing a registration statement are also permitted as long as the communications do not reference an offering. (Rule 163A) Additional safe harbors are available to well-known seasoned issuers (“WKSIs”), which are permitted to engage at any time in oral and written communications, including use at any time of free writing prospectuses, subject to certain conditions and, in specified cases, filing with the SEC. (Rule 163)

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<sup>2</sup> See Securities Act Release No. 33-3844 (October 8, 1957).

All reporting issuers may publish forward-looking information as well as regularly released factual business information. (Rule 168)

Simple announcements of proposed offerings are exempt communications under Rule 135. In addition, a broad category of routine communications regarding issuers, offerings, and procedural matters, such as communications about the schedule for an offering or about account-opening procedures, are permitted pursuant to Rule 134.

Analysts' research reports are permitted in accordance with Rules 137, 138 and 139.

In April 2012, the Jumpstart Our Business Startups Act ("JOBS Act") established a new category of issuer called an emerging growth company ("EGC"), which is allowed to engage in communications with potential investors that are qualified institutional buyers ("QIBs") or institutional accredited investors ("IAIs"),<sup>3</sup> in order to gauge interest in a securities offering ("test-the-waters"), either prior to or following the filing of a registration statement, without those communications being deemed "offers" in violation of Section 5 of the Securities Act. The JOBS Act also allows a broker-dealer to publish or distribute research reports regarding securities of an EGC. Further, the JOBS Act directed the SEC to promulgate rules eliminating the prohibition of general solicitation in connection with private offerings under Rule 506 of Regulation D and Rule 144A, which became effective in September 2013.

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<sup>3</sup> QIBs and IAIs are defined in Rule 144A and Rule 501(a), respectively, under the Securities Act.

### *Which section of the Securities Act governs offering-related communications?*

Section 5(c) of the Securities Act prohibits all "offers" in any form prior to the filing of a registration statement. After the filing of a registration statement, it is a violation of Section 5(b)(1) to make written offers other than by means of a prospectus that meets the requirements of Section 10 of the Securities Act. An example of a prospectus that complies with Section 10 is a preliminary prospectus (the first prospectus distributed to investors prior to a new issuance of a security that contains an indicative price for the security). Section 5(b)(2) prohibits the delivery of a security unless accompanied or preceded by a Section 10 prospectus.

### *What is "gun jumping" and what are its consequences?*

Section 5 violations are commonly referred to as "gun jumping," as the offeror is making an offer before a Section 10 prospectus is required and available. Gun jumping can have business and legal consequences. If the SEC becomes aware of gun jumping, it can take any of a number of actions including:

- withholding effectiveness of the registration statement until the effects of such gun jumping activity have dissipated (an imposed "cooling off period");
- requiring the issuer to file such communications as part of the registration statement, resulting in Securities Act liability for such statements;
- requiring that the gun jumping underwriter be excluded from the offering; and
- assessing administrative penalties against all persons responsible for such activity.

In addition, every purchaser of the security that was subject to an illegal offer has a rescission right for a period of one year.

*How does the nature of the issuer affect its communications?*

For communications purposes, there are primarily five types of issuers:

- **WKSI** – generally, a reporting company that meets the registrant requirements for use of a registration statement on Form S-3 (or Form F-3), is not an “ineligible issuer” (defined below), and
  - has worldwide market value (public float) of its outstanding voting and non-voting common equity held by non-affiliates of \$700 million or more;  
*or*
  - has issued in the last three years at least \$1 billion aggregate principal amount of non-convertible securities, other than common equity, in primary offerings for cash (and not in exchange) registered under the Securities Act, and will register only non-convertible securities other than common equity.
- **Seasoned issuer** – generally, a reporting company that meets the registrant requirements for use of a registration statement on Form S-3 (or Form F-3) and
  - has a public float equal to \$75 million,  
*or*

- is offering non-convertible securities, other than common equity, for cash, provided the issuer:
  - has issued at least \$1 billion in non-convertible securities, other than common equity, in primary offerings for cash (not exchange) registered under the Securities Act, over the prior three years; *or*
  - has outstanding at least \$750 million of non-convertible securities, other than common equity, issued in primary offerings for cash, not exchange, registered under the Securities Act.

- **Unseasoned reporting issuer** – generally, a reporting company that is not a WKSI or a seasoned issuer.
- **EGC** – an issuer with total gross revenues of under \$1.07 billion (adjusted from \$1 billion in March 2017, and subject to inflationary adjustment by the SEC every five years) during its most recently completed fiscal year. An issuer that qualifies as an EGC will remain an EGC until the earliest of:
  - the last day of the fiscal year during which the issuer’s total gross revenues exceed \$1.07 billion; or
  - five years from the issuer’s initial public offering (“IPO”); or

- the date on which the issuer has sold more than \$1 billion in non-convertible debt; or
- the date on which the issuer becomes a large accelerated filer (*i.e.*, has a public float of \$700 million).

For communications not expressly permitted by the JOBS Act, an EGC will have the same status as an unseasoned reporting issuer.

- **Non-reporting issuers.**

Varying restrictions apply to different categories of issuers. WKSIs have the most freedom to communicate at any time as they are widely followed issuers who are also likely to have a regular dialogue with investors and market participants through the press and other media. In the SEC's view, WKSI communications are subject to scrutiny by investors, the financial press, analysts and others who evaluate disclosure when it is made, making it harder for communications by or about such issuers to manipulate the market.

Certain rules also apply to "voluntary" filers, which are issuers that file with the SEC for contractual or other reasons but not because they trigger regulatory filing requirements.

***What is an "ineligible issuer"?***

Rule 405 under the Securities Act defines an ineligible issuer as one that:

- is not current in its reporting obligations under the Exchange Act (with exceptions for certain current reports on Form 8-K);

- within the past three years, is or was a blank check, shell or penny stock company;<sup>4</sup> or
- is the subject of a bankruptcy, criminal, judiciary or administrative proceeding.

Ineligible issuers have very limited use of free writing prospectuses, do not qualify for inclusion in the research reports permitted by the research safe harbors and may not be able to conduct anything but live road shows.

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**General Business Communications**

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***Do the federal securities laws regulate general business communications?***

Ordinary course business communications with customers and suppliers, including advertisements and announcements of new products and services and changes in management are not generally regulated by the federal securities laws and rules. However, depending on whether the issuer is a reporting issuer and the context, such as whether the communication is made shortly before or during an offering, or the timing of an announcement, the federal securities laws may be relevant, as further detailed in these FAQs.

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<sup>4</sup> A blank check company is a development stage company that has no specific business plan or purpose or has indicated its business plan is to engage in a merger or acquisition with an unidentified company or companies, another entity or person. (Securities Act Rule 419(a)(2)). A shell corporation is a company that serves as a vehicle for business transactions without itself having any significant assets or operations. (Securities Act Rule 405). A penny stock issuer is a very small issuer of low-priced speculative securities. (Exchange Act Rule 3a51-1).

***Why should a non-reporting issuer be concerned about the SEC's communications rules?***

A non-reporting issuer should be aware that the federal securities laws apply to its activities even before it files a registration statement for an IPO. There are also limitations on communications in connection with exempt offerings that apply whether or not the issuer is a reporting company.

Further, for any non-reporting issuer contemplating an IPO, it is good practice during at least the year prior to beginning the IPO process to issue factual and even forward-looking information about its business on a regular basis in order to develop a record of making such releases as well as to become more comfortable with SEC requirements and the available safe harbors for such information. It takes time to understand the nature of disclosure requirements as well as the process of releasing information to the public – suppliers, customers and other non-investors – in an SEC-compliant manner.

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**Offering-Related Communications**

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***How did Securities Offering Reform affect communications?***

For many years prior to 2005, the SEC modernized the securities offering process through incremental changes. In 2005, the SEC adopted new rules relating to the securities offering process,<sup>5</sup> referred to as “Securities Offering Reform,” which significantly changed existing registration, communication and offering processes for issuers, and also amended the existing categorization of issuers. The new rules also revised disclosure

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<sup>5</sup> Securities Offering Reform, Securities Act Release No. 33-8591 (July 19, 2005).

regulations relating to securities offerings, resulting in significantly greater flexibility for issuers and other offering participants while explicitly addressing when liability attaches to disclosures. The reforms resulted in the following:

- introduction of the WKSI, which is permitted to communicate freely (without gun jumping concerns) and to file automatically effective shelf registration statements;
- creation of a new communications framework, including the “free writing prospectus,” and expanded offering-related communication safe harbors; and
- redefinition of “written communications” as all communications other than oral communications for Securities Act purposes.

***How has the JOBS Act affected communications?***

The JOBS Act has resulted in the following fundamental changes to offering-related communications by issuers and underwriters:

- An EGC may engage in oral or written communications with QIBs and IAIs in order to gauge their interest in a proposed IPO either prior to or following the first filing of the IPO registration statement.
- The JOBS Act permits a broker-dealer to publish or distribute a research report about an EGC that proposes to register or is in registration, and the research report will not be deemed an “offer” under the Securities Act even if the broker-dealer will participate or is participating in the offering. The JOBS Act also prohibits any self-regulatory organization (“SRO”), such as FINRA, and the SEC from

adopting any rule or regulation that would restrict a broker-dealer from participating in certain meetings relating to EGCs.

- Post-offering, no SRO or the SEC may adopt any rule or regulation prohibiting a broker-dealer from publishing or distributing a research report or making a public appearance with respect to the securities of an EGC. This does away with the traditional post-IPO “quiet period” for EGCs.
- The SEC was directed to revise Rule 506 under Regulation D to relax the prohibition against general solicitation or general advertising contained in Rule 502 in the context of certain Rule 506 private offerings, provided that all purchasers in the offering are accredited investors. Rule 506(c) implementing this change became effective in September 2013.
- The SEC was directed to revise Rule 144A to permit the use of general solicitation or general advertising. Effective September 2013, Rule 144A was amended to eliminate references to “offer” and “offeree,” and as a result, Rule 144A requires only that the securities are sold to a QIB or to a purchaser that the seller and any person acting on behalf of the seller reasonably believe is a QIB. Thus, resales of securities pursuant to Rule 144A can be conducted using general solicitation.

***Does Regulation FD apply to communications made in connection with offerings?***

Regulation Fair Disclosure, or FD, prohibits the *intentional* disclosure of material non-public information regarding an issuer or its securities to select categories

of people, such as broker-dealers, investment advisers, investment companies and investors. In addition, if an issuer *unintentionally* discloses material non-public information to persons covered by Regulation FD, the issuer must publicly disclose the information promptly. Such public disclosure obligations are not triggered by disclosure to persons who expressly agree to keep the disclosed information confidential. The public disclosure obligations under Regulation FD do not apply generally to disclosures in “connection with a securities offering registered under the Securities Act.”<sup>6</sup> Thus, in certain instances, such as communications prior to commencement of an offering, Regulation FD would be applicable in addition to the rules discussed in these FAQs. For additional information about Regulation FD, see Frequently Asked Questions About Regulation FD, available at

<http://media.mofo.com/files/Uploads/Images/FAQs-Regulation-FD.pdf>.

***What is the general framework for the communications rules for registered offerings?***

SEC rules on communications follow the three stages of a registered offering – the pre-filing period, the period prior to the SEC declaring the registration statement effective, which includes the offering itself (the “waiting period”), and after the offering. It should be noted that while the SEC focuses on the filing and effectiveness of a registration statement, the filing and even the effectiveness of a “shelf” registration statement, which is intended to register securities that may be offered in the future by the registrant, is not necessarily the

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<sup>6</sup> In the Release adopting Regulation FD, the SEC stated: “We believe that the Securities Act already accomplishes most of the policy goals of Regulation FD for purposes of registered offerings....” See Release Nos. 33-7881, 34-43154 (August 15, 2000).

commencement of an offering, and the rules described below must be reviewed carefully.

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### Communications Before an Offering

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#### *What communications are permitted prior to an offering?*

Rule 163A under the Securities Act is a safe harbor available to all issuers, even non-reporting issuers and voluntary filers, for certain communications made more than 30 days prior to the filing of a registration statement. Communications occurring more than 30 days prior to filing of a registration statement are not considered pre-filing offers prohibited by Section 5(c) of the Securities Act and will, therefore, be free from gun jumping concerns. Such communications are also not considered to be free writing prospectuses and are not required to be filed with the SEC.

A communication made pursuant to Rule 163A must satisfy the following conditions:

- the communication cannot refer to the securities offering that is the subject of the registration statement;
- the communication must be authorized and made by the issuer; and
- the issuer must take “reasonable steps within its control” to prevent further distribution of the information during the 30-day period prior to filing the registration statement.

The Rule 163A safe harbor may not be used in connection with certain types of business combination transactions, offerings to employees registered on Form S-8, and offerings by ineligible issuers. This safe harbor is also not available for communications

regarding offerings made by a registered investment company or a business development company.

#### *May a WKSI make offers before a registration statement is filed?*

Yes. Rule 163 under the Securities Act is a non-exclusive exemption for WKSIs from the prohibition on making offers prior to filing a statutory prospectus under Section 10 of the Securities Act. This rule allows WKSIs to engage in unrestricted oral and written offers before filing a registration statement. Under Rule 163, an offer by a WKSI before filing a registration statement is free from Section 5(c) restraints, provided that certain conditions are met, including that the written communication:

- contains a prescribed legend;
- is filed with the SEC promptly upon filing a registration statement for the offering; and
- does not relate to “ineligible offerings,” such as certain business combination transactions.

A written offer under Rule 163 is considered to be a statutory prospectus that is subject to liability under Section 12(a)(2) of the Securities Act, and a free writing prospectus that must be filed pursuant to Rule 433. If no registration statement is filed, however, a Rule 163 communication will not need to be filed. Rule 163 communications will not automatically be subject to Section 11 liability because a free writing prospectus is not deemed to be part of a registration statement for Section 11 liability purposes. See “*What liability provisions apply to free writing prospectuses?*” below.



***May underwriters and other offering participants rely on Rules 163 and 163A?***

Underwriters or other offering participants may not rely on either Rule 163 or Rule 163A. Communications under Rules 163 and 163A must be made “by or on behalf of” an issuer. Rule 163 provides that a communication is made “by or on behalf of” an issuer if the issuer or an agent or representative of the issuer, other than an offering participant who is an underwriter or dealer, authorizes or approves the communication before it is made. As a result, the availability of the Rule 163 exemption has been narrowly limited to issuer communications, significantly restricting the ability of a WKSI to conduct any meaningful pre-marketing activities in advance of filing an automatically effective shelf registration statement. Although in 2010 the SEC proposed amendments to Rule 163 to permit underwriters to pre-market WKSI offerings (before any registration statement is filed), the proposal has been tabled. It should also be noted that Rule 163A specifically requires no mention of the offering, thus, eliminating the ability of an underwriter to make any meaningful communication.

***May an EGC communicate with investors prior to filing a registration statement?***

Yes. The JOBS Act allows an EGC to gauge potential interest in a securities offering prior to the filing of a registration statement from QIBs and IAs only. It is difficult to determine whether a standard process or form for these “test-the-waters” communications will develop but it is advisable for the EGC to consult with counsel and its underwriters to ensure that such communications are consistent with its registration statement. The SEC has not announced any plans to

amend Rule 163A or other rules to address the ability of an EGC to “test-the-waters” as this provision of the JOBS Act was effective immediately.

***May an issuer announce a proposed registered public offering?***

Rule 135 permits an issuer or a selling security holder to announce a proposed registered public offering without such notice constituting an illegal offer under Section 5 of the Securities Act. The Rule 135 notice can contain the name of the issuer, the title, amount and basic terms of the securities to be offered, and a brief statement of the manner and purpose of the offering. The Rule permits additional disclosure relating to offerings to existing security holders, including for rights offerings, offerings to employees, exchange offers and Rule 145(a) offerings. A Rule 135 notice cannot identify the managing underwriters.

***Is there a safe harbor for information about foreign offerings?***

Rule 135e permits foreign private issuers, selling security holders, their representatives (including an underwriter<sup>7</sup>) and foreign government issuers to provide journalists with access to information that discusses a present or proposed offering of securities. This rule can be used if the following conditions are met:

- the information must be provided at a press conference or in meetings or written materials held outside the United States;
- the offering is not conducted solely in the United States;

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<sup>7</sup> See Securities Act Release No. 33-7470 (October 10, 1997).

- access is provided to both U.S. and foreign journalists; and
- press-related materials:
  - contain the specific legends that are appropriate to an offering in the United States;
  - if there is an intention to register the offering in the United States, contain a statement of that intention; and
  - do not include a purchase order or coupon in the materials.

The Rule 135e adopting release states that one-on-one interviews held outside the United States are covered by this safe harbor.<sup>8</sup> Investor calls are also covered by this safe harbor as long as the participants are all outside the United States.<sup>9</sup>

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### Communications During an Offering

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#### *May an issuer continue to release factual and forward-looking information?*

Rule 168 under the Securities Act generally permits reporting issuers to continue publishing or disseminating “regularly released factual business and forward-looking information,” even around the time of a registered offering. This safe harbor is designed to permit ongoing communications with the market, such as press releases, earnings releases, conference calls, earnings guidance, and other information released in

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<sup>8</sup> *Id.*

<sup>9</sup> In addition to Rules 135, 135a, 135c and 135e, Rule 135a addresses certain “generic advertising” by investment companies, and Rule 135b addresses options disclosure that meets the requirements of Rule 9b-1 of the Exchange Act by a broker-dealer prior to execution of any order to buy or sell an options contract.

accordance with an issuer’s past practices, but cannot contain information about a potential offering and cannot be made as part of the offering process. These communications will not be deemed to constitute an offer to sell a security that is the subject of an offering pursuant to a registration statement that the issuer proposes to file, or has filed, or that is effective.

Rule 168 is available to any U.S. reporting company and some participants in asset-backed securities transactions. Rule 168 is also available to a foreign private issuer that meets the following conditions:

- satisfies all of the requirements for use of a Registration Statement on Form F-3 (other than reporting history); and
- either
  - has a public float of at least \$75 million; *or*
  - is issuing non-convertible securities and either has (i) issued at least \$1 billion in non-convertible securities, other than common equity, in primary offerings for cash, not exchange, registered under the Securities Act, over the prior three years; or (ii) has outstanding at least \$750 million of non-convertible securities, other than common equity, issued in primary offerings for cash, not exchange, registered under the Securities Act;<sup>10</sup> *and*
- either its equity securities have been listed on a designated offshore securities market for at least 12 months or has a worldwide common

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<sup>10</sup> See *supra*, note 5.

equity market value held by non-affiliates of at least \$700 million.

Rule 168 is not available to non-reporting issuers, who may rely on Rule 169.

An issuer must satisfy additional conditions before availing itself of the Rule 168 safe harbor, including:

- the issuer must have previously released factual information in the ordinary course of business; and
- the timing, manner and form of information must be consistent with prior practice.

New types of financial information cannot be released in anticipation of an offering, and the issuer should not use new methods to release factual business information.

Rule 168 applies to information released on a regular basis and on an unscheduled or episodic basis. In deciding whether the safe harbor is available, the threshold question to consider concerns the nature of the event triggering the release of information.

*May a non-reporting issuer or a voluntary filer continue to release factual business information after commencing an offering?*

A non-reporting issuer (but one that has filed a registration statement for an offering) can continue to release factual information pursuant to the Rule 169 safe harbor. The information that can be released in reliance on this safe harbor is not as broad as under Rule 168 and excludes dividend notices and forward-looking information. The information released under this safe harbor must be widely disseminated and must be intended for use by a non-investor audience, such as suppliers and customers.

*What is a Rule 134 notice and when is it used?*

Rule 134 allows issuers to make certain written communications regarding an offering after a Section 10 prospectus is filed. Rule 134 allows inclusion of the following information:

- certain basic factual information about the identity and corporate location of the issuer, including contact information, and business segments;
- information about the securities offered, such as the title of the securities or amounts being offered;
- a brief description of the business of the issuer;
- a brief description of the intended use of proceeds;
- the name, address, phone number and email address of the distributor of communications regarding the securities being offered, and the fact that it is participating in the offering;
- the names of the underwriters in the syndicate;
- an anticipated schedule for the offering;
- marketing events information;
- a description of the procedures by which underwriters will conduct the offering;
- a description of the procedures for opening accounts and submitting indications of interest;
- information regarding the selling security holders, such as their names and email addresses;
- whether, in the opinion of counsel, the securities are a legal investment for savings banks, fiduciaries, insurance companies or similar investors under the laws of any state or

territory or the District of Columbia, and the permissibility or status of the investment under the Employee Retirement Income Security Act of 1974;

- whether, in the opinion of counsel, the securities are exempt from specified taxes, or the extent to which the issuer has agreed to pay any taxes with respect to the securities;
- whether the securities are being offered through rights issued to security holders and pertinent details thereof;
- the exchanges where the securities will be listed, the ticker symbols, and the CUSIP number assigned to the securities; and
- required legends.

After a preliminary prospectus has been filed containing a price range in the case of IPOs, a Rule 134 notice can include pricing information, including, in the case of debt securities, the final or anticipated maturity, interest rate and yield provisions. A detailed term sheet cannot be included in a Rule 134 notice; however, it may be included in a free writing prospectus.

If the registration statement is not yet effective, Rule 134(b) requires a legend stating that the registration statement is not effective and the name and address of a person from whom a written prospectus for the offering may be obtained.

When Rule 134 requires that the communication be preceded or accompanied by a Section 10 prospectus, that obligation can be satisfied if the communication contains an active hyperlink to such prospectus.

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## Free Writing Prospectuses and Road Shows

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### *What are “written communications” and “graphic communications”?*

Rule 405 under the Securities Act defines a “written communication” as:

- any written or printed communication;
- any radio or TV broadcast (regardless of how transmitted); or
- any “graphic communication.”

“Graphic communication” is defined to include all forms of electronic media, except for a communication that, at the time of the communication, originates live, in real time to a live audience and does not originate in recorded form or otherwise as a graphic communication, although it is transmitted electronically. Examples of graphic communications that may be treated as free writing prospectuses include:

- emails;
- websites;
- “blast” voicemail messages; and
- CD-ROMs.

Individual telephone voicemail messages from live telephone calls, as well as live road shows, will not be considered graphic communications. Subsequent electronic retransmission of these communications, however, will be considered graphic communications and, therefore, would be free writing prospectuses.

### *What is a free writing prospectus?*

Rule 405 under the Securities Act defines a free writing prospectus as, unless the context requires otherwise, any “written communication” that constitutes an offer

to sell or a solicitation of an offer to buy securities relating to a registered offering, that is used after a registration statement has been filed (or, in the case of a WKSI, whether or not such registration statement is filed). A preliminary or final prospectus is not a free writing prospectus. Similarly, a communication delivered after effectiveness of a registration statement that is accompanied or preceded by a statutory prospectus is not a free writing prospectus. Communications that are not considered offers or prospectuses, such as Rule 134 or Rule 135 communications, communications benefiting from the Rule 168 or 169 safe harbors, and research reports are also not considered to be free writing prospectuses.

Free writing prospectuses are primarily governed by Rule 164 and Rule 433 under the Securities Act.

#### ***Who may use a free writing prospectus?***

The ability to use a free writing prospectus depends primarily on whether the issuer is a WKSI, seasoned issuer, unseasoned issuer, non-reporting issuer or ineligible issuer.

A WKSI may use a free writing prospectus for an offering at any time (*see "May a WKSI make offers before a registration statement is filed?"* above).

A seasoned issuer may use a free writing prospectus at any time after the registration statement is filed; there is no requirement to deliver a Section 10 prospectus with or in advance of a free writing prospectus.

For unseasoned issuers and non-reporting issuers, free writing prospectuses can be used at any time after filing a statutory prospectus. In addition, the statutory prospectus must precede or accompany the free writing prospectus, subject to two exceptions. Once a statutory prospectus is filed, if there are no material changes

between the free writing prospectus and the most recent statutory prospectus, there is no need to deliver an additional statutory prospectus. In addition, a statutory prospectus need not be delivered if a free writing prospectus is not prepared by the issuer or an offering participant and is published by a third party.

An ineligible issuer may use a free writing prospectus but it must contain only a description of the terms of the offering, such as a term sheet.

#### ***When may a free writing prospectus be used?***

Rule 164 under the Securities Act provides that once a registration statement has been filed, the issuer or other offering participant can use a free writing prospectus if the issuer is not an ineligible issuer, the offering is an eligible registered offering and, with respect to road show materials, the additional conditions of Rule 433 are met. Registered offerings that do not qualify for use of a free writing prospectus are offerings involving certain business combinations as well as offerings on Form S-8.

#### ***What information may be included in a free writing prospectus?***

A free writing prospectus may include information that is not included in the registration statement. However, the information in the free writing prospectus must not conflict with the information in the registration statement that has been filed nor may it conflict with any Exchange Act reports that are incorporated by reference into the registration statement.

A free writing prospectus must include an appropriate legend that advises the investor to read the issuer's registration statement and SEC filings and provides a

toll-free number that can be used to obtain a copy of the prospectus.

***What are the filing requirements for free writing prospectuses?***

Generally, an issuer must file a free writing prospectus with the SEC no later than the day that it is used. If the free writing prospectus contains information about the final terms of the offering, it must be filed within two business days of first use or the establishment of the terms. The exceptions to this rule are discussed in *“What is a road show and when does it need to be filed?”* below.

An “issuer free writing prospectus” is defined as a free writing prospectus prepared by or on behalf of the issuer, used or referred to by the issuer, containing material information about the issuer or its securities provided by or on behalf of the issuer and a description of the final terms of the issuer’s securities. When an issuer authorizes the use of information or the communication, it is considered to be an issuer free writing prospectus and subject to filing.

Underwriters and offering participants other than the issuer also have filing obligations if they distribute a free writing prospectus in a manner that is designed to lead to a broad unrestricted dissemination. For example, the filing condition applies if an underwriter includes a free writing prospectus on an unrestricted website or provides a hyperlink from an unrestricted website to information that would be a free writing prospectus. Another example of when the filing condition applies is when an underwriter sends out a press release regarding the issuer or the offering that is a free writing prospectus.

***Does information on a website constitute a free writing prospectus?***

Rule 433 under the Securities Act provides that offers of securities that are contained on an issuer’s website or hyperlinked from the issuer’s website are considered free writing prospectuses and need to be filed with the SEC. Historical information located separately and not incorporated by reference into an SEC filing and earnings releases may also qualify for the safe harbor if they meet the Rule 168 or Rule 169 requirements.

***What is a media free writing prospectus and must it be filed?***

Any written offer of securities that is approved or authorized by an issuer, even if it is prepared and distributed by a third party, is considered a media free writing prospectus and needs to be filed. The obligation to file a media free writing prospectus depends on whether the issuer paid for the article to be published or whether the article was published independently.

If the issuer or underwriter authorized the article, it is considered a free writing prospectus, subject to the legend, delivery and filing requirements. The filing must include information about the issuer, its securities, the offering and a copy of the article. If the issuer reasonably believes that information in the article needs to be updated or corrected, the issuer may include that information in the filing.

If the issuer or underwriter did not authorize the article and did not pay for publication, there is no legend or Section 10 prospectus delivery requirement but the article has to be filed within four business days of the issuer or underwriter becoming aware of such publication. An issuer is allowed to correct in such filing any information in the press coverage. The issuer

may also file a copy of the materials published, including transcripts of interviews.

***What is a road show and when does it need to be filed?***

During the offering process, an issuer's management may make presentations to invited groups of institutional investors, money managers and other potential investors. This is commonly referred to as a "road show" and is usually organized by the underwriters. WKSIs may conduct a road show at any time. All other issuers can conduct an offering road show only after a registration statement has been filed.

Rule 433 defines a "road show" as an offer that contains a presentation regarding an offering by one or more members of an issuer's management, and includes discussions of the issuer, management and the securities being offered.

A live road show is not considered a written communication or a graphic communication. "Live road shows" include:

- a live, in-person road show to a live audience;
- a live, in real-time road show to a live audience that is transmitted graphically;
- a live, in real-time road show to a live audience that is transmitted to an "overflow room;"
- a webcast or video conference that originates live and in real-time at the time of transmission and is transmitted through video conferencing facilities or is webcast in real-time to a live audience; and
- the slide deck or other written materials used during any such live road show are not considered "written communications" for purposes of Rule 433 unless investors are

permitted to print or take copies of such information.

All other road shows are considered written communications and therefore free writing prospectuses, which may be required to be filed, as discussed below.

In an IPO (specifically, an offering of common equity or convertible equity by a non-reporting issuer), a road show that is a written communication (that is, copies of the slides are distributed to investors or the presentation is retransmitted or otherwise is not considered "live") is considered a free writing prospectus and must be filed with the SEC. However, if the issuer makes at least one version of a bona fide electronic road show available without restriction to any person, there is no filing obligation. The obligation to make the electronic road show generally available is usually satisfied by posting the road show on the issuer's website. A bona fide electronic road show is defined in Rule 433 as a road show that is a written communication transmitted by graphic means (and cannot be merely the transcript of the event). If the issuer uses more than one electronic road show, then the one posted on the website must include the same general information regarding the issuer, management and the securities being offered as contained in other electronic road shows used for the same offering.

Road show "written communications" by reporting issuers are not required to be filed with the SEC. It is common practice for issuers to post their road shows or investor presentations on their websites and update them periodically. Under certain circumstances, particularly if the issuer is concerned with Regulation FD, an issuer may also file or furnish the

road show materials under the cover of a current report on Form 8-K.

There are also “non-deal road shows” in which issuers meet with institutional investors even though no offering is then contemplated. As with offering road shows, the better practice is not to distribute slides to investors; however, even if slides are distributed, they generally are not considered written communications or free writing prospectuses because they are not provided in connection with an offering.

*What are the record retention requirements for free writing prospectuses?*

Rule 433 requires issuers and offering participants to retain all free writing prospectuses used in connection with an offer and that have not been filed for three years from the initial bona fide offering of the securities.

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**Liability for Certain Communications  
During an Offering**

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*What liability provisions apply to free writing prospectuses?*

Free writing prospectuses are not considered part of a registration statement and, therefore, are not subject to Section 11 liability. However, every free writing prospectus, whether or not filed with the SEC, subjects the issuer and other offering participants to Section 12(a)(2) liability. Other anti-fraud provisions such as Section 17(a)(2) of the Securities Act also apply in actions brought by the SEC. The adopting release for these rules notes that oral statements made at road shows are subject to liability regardless of whether they are free writing prospectuses.

*Is there an exception from liability for “immaterial and unintentional” deviations?*

Issuers that do not comply with the conditions set forth in Rule 433 with respect to free writing prospectuses violate Section 5(b)(1) of the Securities Act. However, Rule 164 provides relief for “immaterial or unintentional” deviations. Under Rule 164, a failure to file or a delay in filing a free writing prospectus will not be considered a violation as long as a good faith and reasonable effort was made to comply with the filing requirement and the free writing prospectus is filed as soon as practicable after the discovery of the failure to file. If a required legend is not included, it will not be considered a violation as long as a good faith and reasonable effort was made to comply with the requirement, the free writing prospectus is amended to include the legend as soon as practicable after the discovery of the failure to file and is retransmitted using the same method and directed to the same prospective purchasers to whom the original free writing prospectus was sent.

*Do free writing prospectuses subject an underwriter to liability?*

Rule 159A under the Securities Act provides that an underwriter or other offering participant will not be liable under Section 12(a)(2) to a purchaser unless the underwriter used or referred to the free writing prospectus in offering or selling securities to the person, the underwriter sold securities to the person and participated in the planning for the use of the free writing prospectus by another offering participant to sell securities to the same person, or the underwriter was otherwise required to file the free writing prospectus. In practice, it is essential that underwriters



agree early in the transaction on the permitted free writing prospectuses.

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### Communications Issues Affecting Confidentially Marketed Offerings

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#### *What rules affect the ability of issuer and underwriters to market registered offerings on a confidential basis?*

Since Securities Offering Reform in 2005, issuers have faced extraordinary market volatility, which raises special concerns in capital raising transactions. These concerns include significant execution risk associated with an offering, particularly the potentially adverse impact on an issuer's stock price if an offering is launched but not successfully completed. Further, underwriters have been faced with increased market risk, particularly in markets where there may be significant short selling in the company's securities at or around the time when the offering is publicly announced.

To navigate these risks, underwriters have found it beneficial to engage in pre-marketing activities prior to public announcement of a transaction. During the pre-marketing phase, the underwriters contact a select group of institutional investors on a confidential basis to gauge the potential interest of those investors in the offering. Prospective investors expressing an interest in learning about a potential offering are brought "over the wall" by the underwriter, and are told about the issuer and the offering subject to their agreement to keep the information confidential and not trade on the basis of the information. Following a successful pre-marketing phase, the issuer may choose to publicly announce the transaction and have the underwriters market the securities to a broader group of investors with the

expectation of very quickly (usually in a matter of hours) determining the size and price of the offering.

Under current rules, these sorts of pre-marketed or "wall-crossed" transactions can typically only be completed when a registration statement is on file and effective with respect to the securities to be offered. Logically, an issuer (as opposed to an underwriter) is not in a position to solicit the interest of prospective investors under Rule 163 on a confidential basis without subjecting itself to market risk, principally because any such solicitations would immediately reveal the issuer's identity. *See also "May underwriters and other offering participants rely on Rules 163 and 163A?" above.*

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### Communications After a Registered Offering

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#### *What communications rules apply immediately following an IPO?*

Following an IPO, an issuer has specific obligations with respect to amending its prospectus and filing required periodic and current reports under the Exchange Act. For 25 days following an IPO, aftermarket sales of shares by dealers must be accompanied by the final prospectus or a notice with respect to its availability. If during this period there is a material change that would make the prospectus misleading, the company must file an amended prospectus. Therefore, it is customary for an IPO issuer not to issue significant communications, particularly relating to additional offerings, during this 25-day period in order to avoid amending the prospectus. Further, under FINRA's research rule, FINRA Rule 2241, analysts are required to be "quiet" during specified periods following an IPO, although these quiet periods have been shortened. FINRA recently amended

its rules relating to equity research, which were formally contained in FINRA Rule 2711 and now are contained in FINRA Rule 2241. See “*What are the ‘mandated quiet periods’ under FINRA Rule 2241?*” below.

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**Communications Issues Affecting Exempt  
or Hybrid Offerings**

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***What are the communications issues in Regulation D offerings?***

There are several exemptions from registration that issuers may rely on in order to raise capital. Prior to the promulgation of Regulation D, issuers relied on Section 4(a)(2) of the Securities Act (prior to the JOBS Act, it was Section 4(2)), which provides an exemption from the registration requirements of the Securities Act for transactions by an issuer “not involving a public offering.” As the statute does not define “public offering,” for many years issuers relied on judicial and administrative interpretations. Regulation D, promulgated by the SEC in 1982, provides issuers with a rules-based safe harbor from the Securities Act registration requirements.

If an issuer wishes to rely on Regulation D (other than Rule 506(c)) for an offering, neither the issuer nor any person acting on its behalf, may engage in any form of general solicitation or advertising, such as advertisements, articles, notices or other communications published in newspapers, magazines or similar media or broadcast over television, radio or the Internet. Meetings or seminars whose attendees have been invited by general advertising or general solicitation are also prohibited.

It should be noted that if Regulation D is not available for the private offering, Section 4(a)(2) may still be

available provided that there has not been any general solicitation that could be deemed to cause the offering to be a “public offering.”

***May an issuer announce a proposed non-registered offering?***

A reporting company may issue a notice pursuant to Rule 135c about an unregistered offering. The notice can be in the form of a news release, a written communication to security holders or employees or other published statements about an unregistered offering. The Rule 135c notice can contain the name of the issuer, the title, amount and basic terms of the offering, the time of the offering, a statement as to the manner and purpose of the offering without naming the underwriters and other specific information relating to the type of offering. Prior to the adoption of Rule 506(c) and for any private offering not involving general solicitation, this kind of notice was more likely to be used after an unregistered offering had been priced or sold but before the offering closed because this rule generally created tension with the SEC’s prohibition on general solicitation in connection with non-registered offerings.<sup>11</sup> However, an issuer conducting a Rule 506(c) or Rule 144A offering may use a press release that does not comply with Rule 135c.

A Rule 135c notice must be filed with the SEC on a current report on Form 8-K (domestic) or report on Form 6-K (foreign private issuer), as applicable.

Rule 135c is also available for foreign private issuers that are exempt from registration under the Exchange Act pursuant to Rule 12g3-2(b); any Rule 135c notice is

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<sup>11</sup> See, e.g., Rule 502(c) under the Securities Act. But see “*How has Rule 506 been revised to permit “general solicitation,” as required by the JOBS Act?*” below.

furnished to the SEC in accordance with Rule 12g3-2(b). Rule 135c is not available for non-reporting issuers.

*How has Rule 506 been revised to permit “general solicitation,” as required by the JOBS Act?*

Title II of the JOBS Act directed the SEC to eliminate the ban on general solicitation and general advertising in Rule 502(c) for certain offerings under Rule 506 of Regulation D under specified conditions. Rule 506 is the most popular means for conducting a private offering because it permits issuers to raise an unlimited amount of money and preempts state securities laws. This change to Rule 506, as well as the change to Rule 144A, are available to all issuers, not just EGCs, as well as private companies and funds. The JOBS Act specifies that any offering made pursuant to Rule 506(c) that uses general advertising or general solicitation will not be deemed a “public offering.”

As required by the JOBS Act, the SEC adopted Rule 506(c), effective September 2013, which permits the use of general solicitation and general advertising, subject to the following conditions:

- the issuer must take reasonable steps to verify that the purchasers of the securities are accredited investors; the SEC’s Staff indicated that “reasonable efforts” to verify investor status will be an objective determination by the issuer based on the SEC’s principles-based guidance;
- all purchasers of securities must be accredited investors, either because they come within one of the enumerated categories of persons that qualify as accredited investors or the issuer reasonably believes that they qualify as

accredited investors, at the time of the sale of the securities; and

- the conditions of Rule 501 and Rules 502(a) and 502(d) are satisfied.

At the same time as the SEC adopted Rule 506(c), it also issued proposals<sup>12</sup> to amend Regulation D and Form D to address some of its concerns regarding the impact of general solicitation on the private offering process and provide the SEC with additional information about the Rule 506(c) process, including the following:

- an issuer would be required to file a Form D not later than 15 calendar days from the commencement of general solicitation efforts and a final amendment within 30 days after the completion of such an offering.
- Form D would request additional information about the issuer, the offered securities, the use of proceeds of the offering, the types of general solicitation that were used, and the methods used to verify investor status.
- Rule 507 would be amended to promote compliance with the Form D filing requirement by implementing certain disqualification provisions to the extent that the issuer and its affiliates failed to comply with Form D filing requirements.
- Proposed Rule 509 would require an issuer to include certain legends on any written general solicitation materials regarding type of offering, nature of investors and risks.

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<sup>12</sup> See Securities Act Release No. 33-9416 (July 10, 2013), available at <http://www.sec.gov/rules/proposed/2013/33-9416.pdf>.

- For a temporary two-year period, issuers would be required to file with the SEC any written solicitation materials, which would not be publicly available.
- The proposal also solicits comment on the definition of “accredited investor” and requests comment on whether there should be additional requirements relating to the communications used in general solicitation.

The SEC has not announced any timing for adopting or amending these proposals.

*Is there a definition of “general solicitation” or has the Staff of the SEC provided guidance regarding the types of communications that would be viewed as a general solicitation?*

After the adoption of the final rules relaxing the prohibition against general solicitation for Rule 506(c) offerings, there was considerable debate regarding the types of communications that would constitute a “general solicitation.” It was well understood that the SEC would interpret the term broadly and that the term would encompass communications relating to an offering of securities that were not directed at specific individuals or entities with which the issuer or a financial intermediary acting on the issuer’s behalf had a pre-existing substantive relationship.

Over the years, the Staff of the SEC had provided guidance regarding the types of activities that were sufficient to establish a relationship prior to an offering of securities being made. In 2015, the Staff of the SEC’s Division of Corporation Finance provided guidance in the form of a number of Compliance & Disclosure Interpretations (C&DIs) that reaffirmed longstanding principles relating to the types of communications that

would or would not be viewed as constituting a “general solicitation.” The C&DIs reiterate that regularly released factual business communications would not be considered a general solicitation. Presentations at business plan competitions and the like should be evaluated and considered based on the facts and circumstances. If there is no mention made of a securities offering or the attendees are known to the issuer or confirmed to be sophisticated investors, one might conclude that there is no general solicitation. Communications that are directed to persons with whom the issuer or its agent has a pre-existing substantive relationship also would not be considered to be a general solicitation. Of course, by contrast, unrestricted communications relating to an offering made using the internet would constitute a general solicitation. The C&DIs also address certain questions relating to establishing a substantive relationship prior to making an offer of securities. The Staff of the SEC also addressed the establishment by a registered investment adviser of a pre-existing substantive relationship in a recently issued no action letter.

Source: Compliance and Disclosure Interpretations (“C&DIs”), Securities Act Rules, questions 256.29 to 256.32. *See also* Citizen VC, Inc. (Aug. 6, 2015), available at <https://www.sec.gov/divisions/corpfin/cf-noaction/2015/citizen-vc-inc-080615-502.htm>. *See our* Practice Pointers on Navigating the Securities Act’s Prohibition on General Solicitation and General Advertising at <https://media2.mofo.com/documents/160600practicepointersgeneralsolicitation.pdf>.

*Is general solicitation available for other resales of securities?*

The JOBS Act lifting of the prohibition on general solicitation applies only to Rule 506 and Rule 144A. Rule 506(c) is available only to issuers. Thus, general solicitation is not permitted in connection with a resale of securities under Section “4(a)(1-1/2)” (the practice-created interplay of Section 4(a)(1) and Section 4(a)(2) exemptions).

The Fixing America’s Surface Transaction Act (the “FAST Act”), enacted on December 4, 2015, incorporates the provisions of the Reforming Access for Investments in Startup Enterprises Act (“RAISE Act”) that codify a new resale exemption, Section 4(a)(7) under the Securities Act (the “Section 4(a)(7) exemption”). The Section 4(a)(7) exemption became effective immediately after the FAST Act was signed into law. The Section 4(a)(7) exemption, which exempts certain accredited investor transactions involving unregistered resales, is not available if general solicitation is used.

*Will the use of general solicitation in a Rule 506(c) offering affect whether there has been “gun jumping” in a subsequent IPO?*

Issuers and their counsel have generally gotten comfortable that a private placement pursuant to Section 4(a)(2) or Rule 506(b) shortly before the filing of an IPO is not likely to be considered gun jumping (*see “What is ‘gun jumping’ and what are its consequences?”* above) because there is no general solicitation. However, an issuer conducting a Rule 506(c) offering in close proximity to the filing of an IPO might be more problematic, given that the general solicitation (especially if the Rule 506(c) offering involves the sale of the same security as that offered in the IPO) may be

viewed as “gun jumping.” Further, in the case of EGCs, the JOBS Act specifically permits test-the-waters communications with QIBs and IAIs prior to or after the filing of a registration statement; however, general solicitation used in a Rule 506(c) offering may also raise concerns for any test-the-waters discussions.

*What precautions should a placement agent take in a private financing transaction?*

The placement agent should place the appropriate legends on the private placement memorandum that is given to investors. The placement agent should carefully track the number of investors contacted and who have received the private placement memorandum. If the placement agent uses electronic methods to disseminate the private placement memorandum, the document should be sent in a read-only pdf document and the recipients must be alerted to the confidential nature of the information with the appropriate legends.

*Do the safe harbors offered by Rules 137, 138 and 139 for analysts’ research reports apply to private placements?*

The safe harbors offered by Rules 137, 138 and 139 apply to private placements. Rule 137 is available only to broker-dealers that are not participants in the offering and applies to most issuers, including non-reporting issuers.

Rule 138 permits a broker-dealer participating in a distribution of securities of an issuer to publish research reports about that issuer if certain conditions are met. Rule 139 permits a broker-dealer participating in a distribution of securities of an issuer to publish research reports concerning that issuer or any class of its securities if certain conditions are met. Research reports

permitted by Rules 138 and 139 will not be considered general advertising or solicitation for purposes of Rule 144A offerings, nor will they constitute a directed selling effort or be inconsistent with the offshore transaction requirement for offerings pursuant to Regulation S.

***How can a placement agent prequalify potential investors without violating confidentiality obligations?***

The placement agent should use an investor script to prequalify all potential investors. The script will alert all potential investors that they are receiving confidential information regarding an issuer and a transaction. This script should be given prior to revealing the issuer's name. The placement agent will receive oral confirmation from all potential investors that the information will be kept confidential.

***What are the typical communications in a PIPE offering?***

An issuer is owed a duty of confidentiality from its agents, such as its placement agent, accountants, and other similar participants in the PIPE (Private Investment in Public Equity) process. Generally, an issuer does not share any information with potential investors that has not already been included in the issuer's Exchange Act reports. A private placement memorandum for a PIPE transaction usually contains the issuer's Exchange Act reports, together with legal disclaimers. It is prudent to limit the information contained in the private placement memorandum unless the issuer will be receiving signed confidentiality agreements. Although the issuer is not sharing material nonpublic information about the issuer's business with potential investors, the issuer is sharing its plans

concerning a potential financing transaction. The fact that the issuer is contemplating a PIPE transaction may itself constitute material nonpublic information. The issuer should ensure that, before the placement agent reveals the issuer's name, the placement agent obtains an oral agreement from each potential purchaser it contacts that information shared will be kept confidential. An investor who agrees to keep the information confidential also agrees not to trade on that information. This oral agreement may be documented subsequently through an acknowledgement and a covenant in the purchase agreement.

The ability to use general solicitation in a Rule 506(c) offering will probably not be relevant to a PIPE transaction because, as with confidentially marketed public offerings, the mere announcement of the potential private offering could adversely affect the stock price.

***What is a "cleansing release"?***

If a public company provides material non-public information ("MNPI") to investors or potential investors in connection with a private or exempt offering, the recipients of this information will typically require the issuer to disclose MNPI within a day or less of the offering being priced in order for the recipients to avoid any implication that they are thereafter trading on the basis of or while in possession of MNPI. They are "cleansed" of MNPI; hence, the "cleansing release." The issuer may also be required to file a Form 8-K in order to satisfy its obligations under Regulation D. An obligation to issue a cleansing release can be problematic if the offering does not price, and issuers and potential investors may have significant negotiations over MNPI provided and the obligation to

cleanse. In a Rule 144A offering, an issuer may decide to disclose MNPI before or simultaneously with the commencement of the offering.

***What communications are allowed in a Rule 144A offering?***

Pursuant to the JOBS Act, the SEC was directed to revise Rule 144A to permit the use of general solicitation or general advertising. The SEC adopted amendments to Rule 144A, effective September 2013, to eliminate references to “offer” and “offeree,” and as a result, Rule 144A will require only that the securities are sold to a QIB or to a purchaser that the seller and any person acting on behalf of the seller reasonably believe is a QIB. Thus, resales of securities pursuant to Rule 144A can be conducted using general solicitation, eliminating the restrictions on communications with potential investors, including, for example, the requirements of Rule 135c for press releases. The SEC also has clarified that even where a general solicitation is used in connection with resales under Rule 144A, the private sale made by the issuer to the initial purchaser in reliance on the Section 4(a)(2) exemption is not affected.<sup>13</sup>

Rules 168 and 169 are available to the financial intermediaries acting as “initial purchasers” in respect of a Rule 144A offering. Publication or distribution of a research report is not considered an offer for sale or an offer to sell a security and, therefore, would not violate the current general solicitation or general advertising restrictions of Rule 144A.

Electronic road shows are also permitted in connection with Rule 144A offerings. However, access to the road show must be password-protected, with a separate

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<sup>13</sup> See Securities Act Release No. 33-9415 (July 10, 2013), note 172, available at <http://www.sec.gov/rules/final/2013/33-9415.pdf>.

password for each offering. Passwords may be issued only to those potential purchasers the seller reasonably believes are QIBs, and the seller must not otherwise have knowledge or reason to believe that any such potential purchaser is not a QIB. The SEC has 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).<sup>14</sup>

***What communications are allowed in a Regulation S offering?***

Rules 168 and 169 are available to financial intermediaries in respect of a Regulation S offering. Publication or distribution of a research report does not constitute directed selling efforts. In addition, Rule 135 or 135c notices, 135e notices, and customary communications to shareholders are permitted communications.

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 Regulation S Category 2 or 3 offering) absent registration or

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<sup>14</sup> SEC No-Action Letter, Net Roadshow, Inc. (Jan. 30, 1998); and SEC No-Action Letter, CommScan, LLC (Feb. 3, 1999).

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 or person holding accounts excluded from the Rule 902(k) definition of U.S. person solely in their capacities as holders of those accounts; and
- a tombstone advertisement in a publication having less than 20% of its worldwide circulation in the United States that contains the following:
  - the legend described above and legends required by law or any foreign or U.S. regulatory authority; and
  - limited permitted information, including the issuer's name and a brief indication of its business; terms of the securities to be sold; the name and address of the managing underwriters; the dates on which sales commence and conclude; and whether the offering is pursuant to rights issued to security holders and related information;
- bona fide visits to real estate, plants or other facilities located in the United States conducted for a prospective investor by an issuer, a distributor or any of their respective affiliates;
- 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;

- publication by an issuer of a notice pursuant to Rule 135 or Rule 135c;
- access for any journalist 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 Rule 135e are satisfied; and
- publication or distribution of a research report by a broker or dealer in accordance with Rule 138(c) or Rule 139(b).

The SEC has made it clear that a Regulation S offering will not be integrated with a Rule 506(c) or Rule 144A offering, and that the use of general solicitation will not constitute "directed selling efforts" in respect of the Regulation S offering.<sup>15</sup>

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#### Certain Communications Issues Applicable to Financial Intermediaries

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For additional information on these issues, *see also* our Frequently Asked Questions About Separation of Research and Investment Banking, available at <http://www.mofo.com/files/Uploads/Images/Frequently>

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<sup>15</sup> See Securities Act Release No. 33-9415 (July 10, 2013), at the text accompanying note 177, available at <http://www.sec.gov/rules/final/2013/33-9415.pdf>.



[-Asked-Questions-about-Separation-of-Research-and-Investment-Banking.pdf](#)

***What is a research report?***

Rule 137 defines “research report” as a written communication that includes information, opinions or recommendations with respect to securities or an issuer, *whether or not* it provides information reasonably sufficient for an investment decision.

FINRA Rule 2241 defines “research report” in a slightly different manner, as a “written (including electronic) communication that provides (1) an analysis of equity securities of individual companies or industries, *and* (2) information reasonably sufficient upon which to base an investment decision.”

It is important to note the difference between these two definitions. A publication would be considered a research report, even if an investor could not base an investment decision upon the report, and be subject to the various disclosures required by Rules 137-139 while not being governed by FINRA Rule 2241.

***Are there communications safe harbors available to financial intermediaries?***

Rules 137, 138 and 139 under the Securities Act are designed to protect analysts, brokers and dealers from general solicitation and gun jumping violations in connection with their regularly disseminated research reports. As noted above, there are also limited safe harbors in other rules. In all cases, the broker or dealer must publish research reports on the types of securities or issuers in question in the regular course of business.

***What are the requirements for research reports by broker-dealers not participating in distribution?***

Rule 137 covers distribution of research reports by broker-dealers that are not participating in an offering. A broker-dealer that is not a participant in an offering but publishes or distributes research about an issuer will not be deemed to make offers of a security or to participate in a distribution of those securities as an underwriter. Conditions to the availability of this safe harbor are:

- the broker-dealer must not participate in the offering and must not have received compensation from the issuer, its affiliates or participants in the securities distribution;
- the broker-dealer must publish or distribute the research report in the regular course of business; and
- the issuer is not a blank check company, shell company or a penny stock issuer.

Independent research prepared by a broker-dealer not participating in an offering, but paid for by a broker-dealer participating in the offering, will be considered distributed by an offering participant and will not satisfy the Rule 137 safe harbor. Subscription payments in the ordinary course are permitted.

***What are the requirements for research reports for broker-dealers participating in a distribution of securities not covered by the research report?***

Rule 138 covers publication of research reports by a broker-dealer participating in an offering about securities that are not the subject of the offering, whether a registered offering or an exempt transaction pursuant to Rule 144A or Regulation S. The broker-dealer must publish research reports on the types of

securities in question in the regular course of business. Rule 138 permits a broker-dealer participating in the distribution of an issuer's securities to publish and distribute research reports that either:

- relate solely to the issuer's common stock, debt securities or preferred stock convertible into common stock, where the offering solely involves the issuer's non-convertible debt securities or non-convertible non-participating preferred stock; or
- relate solely to the issuer's non-convertible debt securities or non-convertible non-participating preferred stock, where the offering solely involves the issuer's common stock, debt securities, or preferred stock convertible into common stock.

Rule 138 is available for research reports on all reporting issuers, other than voluntary filers, that are current with their reporting obligations under the Exchange Act. It is also available for reports on a foreign private issuer if such issuer:

- satisfies all of the requirements of Form F-3 (other than reporting history); and
- either
  - has a public float of at least \$75 million; or
  - is issuing non-convertible investment grade securities; and either its equity securities have been listed on a designated offshore securities market for at least 12 months or has a worldwide common equity market value held by non-affiliates of at least \$700 million.

Rule 138 is not available for research reports about voluntary filers and ineligible issuers.

*What are the requirements for research reports for broker-dealers participating in a distribution for securities covered by the research report?*

Rule 139 covers publication of research about the securities being offered by an underwriter. A broker-dealer participating in a registered offering can publish research reports about the issuer and its securities or the issuer's industry or sub-industry without violating Sections 2(10) and 5(c) of the Securities Act; provided the issuer:

- has filed all required Exchange Act reports during the preceding 12 months and meets registrant requirements of Form S-3/F-3, and either:
  - has \$75 million or more in public float;
  - is or will be offering securities that qualify as non-convertible investment grade securities (in accordance with Form S-3/F-3); or
  - is a WKSI; or
- is a foreign private issuer that meets the conditions described above under "*What are the requirements for research reports for broker-dealers participating in a distribution of securities not covered by the research report?*" above.

This rule is not available for research reports about voluntary filers, blank check companies, shell companies and penny stock issuers.

***What are the Rule 139 requirements for issuer-specific reports?***

Under Rule 139, in addition to the issuer requirements, the conditions for a broker-dealer issuing an issuer-specific report are:

- the broker-dealer must publish or distribute research reports in the regular course of its business; and
- such publication or distribution cannot represent either the initiation of publication or the re-initiation of publication.

***What are the Rule 139 requirements for industry-specific reports?***

Industry-specific reports are reports that a broker-dealer publishes in the regular course of business. The publication of the research cannot be initiated prior to the offering. Such reports must contain similar types of information about the issuer or its securities as contained in prior reports. In addition, similar information about other issuers in the same industry or sub-industry is usually included. However, the analysis about the issuer should not be given greater prominence or space in the publication than that given to other issuers.

When a publication contains a projection of a company's sales or earnings, such projections will have to be published on a regular basis, will need to be published with respect to the company in registration and must include information about a substantial number of companies in the company's industry.

***What are the disclosures required under FINRA Rule 2241?***

If a member or a research analyst has a financial interest in the securities of the subject company, then details about such interest must be disclosed. If the member or research analyst owns 1% or more of the securities of the subject company, at the end of the calendar month preceding the publication of the research report, then this fact must be disclosed. Any other conflicts of interest must also be disclosed.

***What are the "mandated quiet periods" under FINRA Rule 2241?***

There are several quiet periods under Rule 2241. For example, no member can publish or distribute a research report and no analyst can make a public appearance for 10 calendar days following an IPO and for three calendar days following a secondary offering. However, the JOBS Act has excluded offerings by EGCs from these requirements. See "*How does the JOBS Act affect FINRA Rule 2241?*" below.

***What are analysts prohibited from doing under FINRA Rule 2241?***

Rule 2241 prohibits a research analyst from:

- participating in a road show relating to an investment banking transaction;
- communicating with a customer in the presence of investment banking personnel or company management about a pending investment banking services transaction; and
- publishing unfair and misleading communications about an investment banking transaction.

*How does the JOBS Act affect FINRA Rule 2241?*

The JOBS Act prohibits any national securities association (which includes FINRA) or the SEC from adopting any rule or regulation prohibiting a broker-dealer from publishing or distributing a research report or making a public appearance with respect to the securities of an EGC within any prescribed period of time following the EGC's IPO or the expiration date of any lock-up agreement. This eliminates the post-IPO "quiet period" for EGCs.

Furthermore, Title I of the JOBS Act allows a broker-dealer assisting in *any* public offering of the common equity securities of an EGC to publish or distribute a research report about the issuer. This research report will not be deemed to be an "offer" under the Securities Act, even if the broker-dealer is or intends to participate in the offering.

The JOBS Act also prohibits a national securities association or the SEC from maintaining rules restricting research analysts from participating in meetings with investment banking personnel and an EGC in connection with an EGC's IPO.

None of the above requirements of the JOBS Act required implementing rules so they were effective immediately.

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