# OPEN IPO

AUCTION DISTRIBUTION METHODOLOGIES

MORRISON & FOERSTER lawyers have played a key role in the design of Open IPO, an innovative Dutch auction securities distribution methodology used by W.R. Hambrecht + Co. The Open IPO auction differs from the traditional method of pricing and distributing initial public offerings by using an ascending price competitive auction to determine both the initial offering price and the allocation of securities being offered.

Before a registration statement relating to an offering becomes effective, but after a preliminary prospectus is made available, the underwriter solicits bids from potential investors. These bids must specify both the price and the number of securities the bidder wishes to purchase. Prior to effectiveness of the registration statement, potential investors are advised that the auction is expected to go "live" in two days and are asked to reconfirm their bids.

After the registration statement becomes effective, potential investors are advised that the auction will close, prior to which they may modify or withdraw their bids. Under certain circumstances, all bids may be required to be reconfirmed. Typically, the auction closes and the public offering price is determined at the close of trading on the Nasdaq National Market on the date of effectiveness. Following the close of the auction, the underwriter determines a "clearing price," or the highest price at which all offered shares can be sold. Once a "clearing price" is set, the issuer and underwriter establish the public offering price. The public offering price may be less than, but cannot exceed, the "clearing price." The actual public offering price will be based, in part, on other factors, such as market conditions and the performance of shares of comparable companies. If more shares are bid for at or above the public offering price than the number of shares offered, the shares are allocated on a pro rata basis without any favoritism being shown to institutional or pre-existing customers of the underwriter.

This distribution methodology is becoming increasingly popular as more issuers become convinced that they may, through the transparency of this method, obtain better pricing and broader allocation of their securities, while incurring less dilution and lower offering costs. Investors have come to appreciate the equal access and fair allocation provided by Open IPO.

The federal securities laws issues and FINRA issues that we addressed in connection with creating this methodology were complex, and in certain instances, novel. We worked with the SEC staff to develop confirmation procedures that provided potential investors with the ability to change or withdraw their bids without disrupting the closing of the auction. We also were able to establish that the unique nature of the auction justified a broader range for the estimated public offering price on the cover of the preliminary prospectus than the range permitted for traditional offerings. We succeeded in convincing the SEC staff that Open IPO was not an “at the market” offering within the meaning of the SEC’s rules and in crafting new disclosure language by which this unique distribution method could be described to potential investors.

Having worked through the legal and regulatory issues necessary to launch the Open IPO auction, we turned our attention to helping WR Hambrecht + Co. develop an auction technology that could be used in follow-on offerings. Unlike Open IPO, OpenFollowOn is a descending price auction in which all shares offered are sold at the highest price at which bids are placed for all of the shares offered. The first OpenFollowOn offering, for Overstock.com, was completed successfully earlier this year.