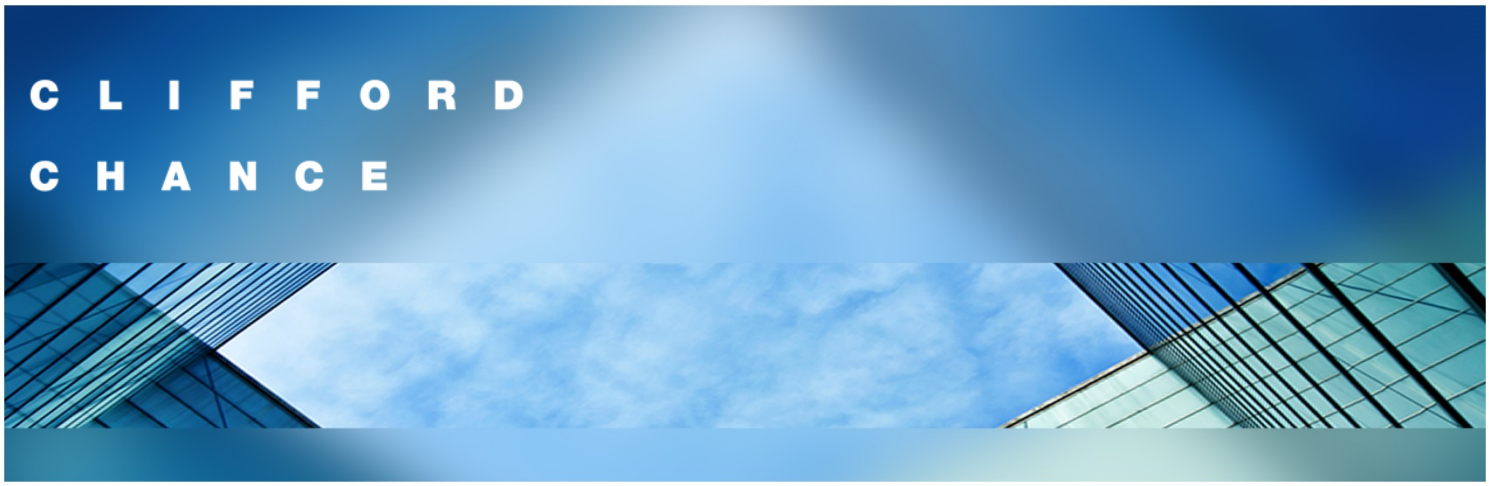

SEC EASES RESTRAINTS ON PRE-MARKETING INVESTOR COMMUNICATIONS

On September 26, 2019, the Securities and Exchange Commission ("SEC") adopted new Rule 163B under the U.S. Securities Act of 1933, as amended (the "Securities Act"), extending the "test-the-waters" accommodation, currently available only to emerging growth companies ("EGCs"), to all issuers (the adopting release is available here). Effective December 3, 2019, Rule 163B will permit all issuers, whether domestic or foreign, reporting or non-reporting, to communicate with certain institutional investors before and after filing a registration statement to gauge market interest in a contemplated public securities offering in the United States. This new rule also allows issuers to authorize others, such as underwriters, to engage in these types of communications on their behalf.

BACKGROUND

Section 5(c) of the Securities Act prohibits issuers or other persons from making oral or written offers until a registration statement is filed with the SEC. Once a registration statement is filed, Section 5(b)(1) limits written offers to a statutory prospectus that complies with Section 10 of the Securities Act.

As part of securities offering reform in 2005, the SEC adopted Rule 163, which permits pre-filing offers for well-known seasoned issuers ("WKSIs") and provides an exemption from Section 5(c) allowing issuers to communicate with potential investors prior to the filing of a registration statement. Notably, Rule 163 is available only to issuers that qualify as WKSIs, and not to underwriters, dealers, or other market participants, limiting its utility. Furthermore, Rule 163 also requires covered written communications to include legends and be filed with the SEC as a free writing prospectus ("FWP"). In addition, Rule 163 does not cover communications involving registered business combination transactions or communications in offerings by registered investment companies or business development companies.

In 2012, Congress passed the Jumpstart Our Business Startups Act (the "JOBS Act"), providing for a new Section 5(d) of the Securities Act allowing an EGC, or any person authorized to act on its behalf, to communicate with qualified institutional buyers ("QIBs") or institutional accredited investors ("IAIs") both before and after the filing of a registration statement. Section 5(d) permits EGCs to evaluate investor interest in a potential registered securities offering without the time and expense associated with the preparation of a registration statement. Test-the-waters materials used by EGCs pursuant to Section 5(d) do not require legends and need not be filed with the SEC as an FWP.

NEW RULE 163B

Rule 163B in effect extends the JOBS Act's accommodation for test-the-waters communications to all issuers. It permits any issuer, including registered investment companies and business development companies, and any person authorized to act on their behalf (including underwriters, dealers, and other participants), before or after filing of a registration statement, to engage in oral or written communications with potential investors that are, or who are reasonably believed to be, QIBs or IAIs.

The table below outlines the key distinctions between Rule 163, Section 5(d) and Rule 163B:

	Rule 163	**Section 5(d)**	**Rule 163B**
Who can use it?	Well-known seasoned issuers only	EGCs and any person authorized to act on their behalf	All types of issuers and any person authorized to act on their behalf
Who can be solicited?	No limitation	QIBs and IAIs	QIBs, IAIs, and any entities reasonably believed to be QIBs or IAIs
Is the communication a free writing prospectus?	Yes	No	No
Is a legend required?	Yes	No	No
Does it need to be filed with the SEC?	Yes	No	No

The provisions of Rule 163B are discussed in further detail below.

Investor status

Rule 163B would permit an issuer to engage in pre- and post-filing communications to gauge investor interest so long as the potential investors are, or the issuer reasonably believes them to be, QIBs or IAIs. A QIB generally is an institution that, acting for its own account or the accounts of other QIBs, in the aggregate, owns and invests on a discretionary basis at least $100 million in securities of unaffiliated issuers. An IAI is any institutional investor that is also an accredited investor, as defined in Rule 501(a) of Regulation D. The SEC specifically declined to extend Rule 163B to investors who are natural persons.

Rule 163B does not specify any particular verification steps or methods for establishing reasonable belief regarding the status of investors. This approach is intended to provide flexibility for issuers to use methods that are appropriate and cost-effective in light of the facts and circumstances of each contemplated offering and each potential investor.

Test-the-waters communications are still "offers" for purposes of the Securities Act

While Rule 163B communications are exempt from Section 5(b)(1) and Section 5(c) of the Securities Act, they will continue to be considered “offers” (as broadly defined in Section 2(a)(3) of the Securities Act) and therefore subject to Section 12(a)(2) liability in addition to the anti-fraud provisions of the federal securities laws.

For purposes of any concurrent or subsequent offshore offerings in reliance on Regulation S, the SEC confirmed in the adopting release for Rule 163B that communications made in compliance with Rule 163B would not constitute "directed selling efforts".

In the SEC's view, however, a Rule 163B communication could constitute a general solicitation, depending on the facts and circumstances regarding the manner in which the communication is conducted. If an issuer chooses to engage in Rule 163B communications prior to, or concurrent with, a private placement for which there should be no general solicitation, the issuer should conduct such communications in a manner that preserves the availability the private placement offering exemption upon which it is seeking to rely.

Regulation FD applies to test-the-waters communications

Issuers subject to Regulation FD should evaluate whether any information in a Rule 163B communication would trigger any disclosure obligation under Regulation FD or whether an exemption under Regulation FD would apply. Regulation FD requires public disclosure of any material nonpublic information that has been selectively disclosed to certain securities market professionals or shareholders if the issuer has a class of securities registered under Section 12 of the U.S. Exchange Act of 1934, as amended (the "Exchange Act"), or is required to file reports under Section 15(d) of the Exchange Act, with an exception for foreign private issuers. Unless an exception applies, covered issuers that selectively disclose material nonpublic information while conducting Rule 163B communications would generally be required to disclose such information publicly under Regulation FD. To avoid liability for insider trading or market manipulation under Rule 10b-5, foreign private issuers generally follow similar disclosure practices. Accordingly, issuers should consider whether a Rule 163B communication contains any material non-public information (e.g., the existence of a possible offering) and, if so, whether such information should be made public or, alternatively, whether potential investors should be required to enter into confidentiality agreements prior to receiving the Rule 163B communication.

Consistency with registration statement

As with other types of securities offering related communications, issuers and their underwriters will want to exercise caution regarding the content of Rule 163B

communications. In the proposing release for Rule 163B, the SEC indicated that information in a Rule 163B communication should not conflict with material information in the related registration statement. In the adopting release, the SEC clarifies that this statement was not meant to create an additional condition to the exemption being available. The SEC also acknowledges that when a Rule 163B communication precedes the filing of a registration statement, circumstances or messaging may change by the time the issuer files the registration statement. In this context, the SEC emphasizes that while statements made in a Rule 163B communication may differ from a subsequently filed registration statement, the Rule 163B communication should not contain any material misstatements or omissions at the time such communication is made.

In addition, the content of a Rule 163B communication should generally not go beyond the information that is expected to be included in the registration statement, and leaving behind any written materials in pre-marketing communications should be discouraged.

No filing or legending requirements

Unlike Rule 163, which conditions exemptive relief for a written communication on the inclusion of a legend and filing of the communication as an FWP, Rule 163B does not require any legending or public filing of a Rule 163B communication. The SEC has also amended Rule 405 to clarify that both Section 5(d) and Rule 163B written communications are excluded from the definition of "free writing prospectus" and from the prospectus filing requirement of Rule 424(b). SEC staff reviewing the related registration statement may request that the issuer furnish any written Rule 163B communications as part of its review, as is currently the practice with Section 5(d) communications.

CONCLUSION

The expanded test-the-waters regulatory relief provided by Rule 163B is the latest in a series of SEC rulemaking accommodations intended to encourage more companies to consider undertaking a registered public offering. The broad availability of the Rule 163B communication exemption provides issuers and other market participants who are not eligible to benefit from the Section 5(d) or Rule 163 communications exemption with an additional tool to evaluate market interest without having to commit the time and expense necessary to undertake a contemplated securities offering.

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