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Integration of Private and Public Offerings 2015

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INTEGRATION OF PRIVATE AND PUBLIC OFFERINGS 2015

I. INTRODUCTION

A. Outline Coverage

This outline reviews the SEC's interpretations that relate to the integration of private and public offerings and the challenges they impose for the capital formation process. The outline also describes current policies of the SEC staff that affect so-called "PIPE" offerings and "private equity lines." It has been updated to reflect the impact of the JOBS Act described below and the SEC's adoption of implementing rules and interpretations under that Act.

B. Recent Developments

On April 5, 2012, the President signed into law the Jumpstart Our Business Startups Act, the JOBS Act, the most significant securities legislation affecting capital raising in many decades. Among other things, the JOBS Act, especially by directing the SEC to amend Rule 506 to permit general solicitation in some circumstances and permitting test-the-waters communications by some companies before or after the filing of a registration statement for a public offering, will have a significant impact on various aspects of the integration analysis for private and public offerings. As directed by the JOBS Act, the SEC has amended Rule 506, effective September 23, 2013, to permit such general solicitation. Also, as directed by the Dodd-Frank Act, the SEC has added, as of such date, "bad actor" disqualification provisions to Rule 506. In addition, the SEC has proposed for comment further changes to Regulation D relating primarily to use of Rule 506. Some of the impacts of these changes are clear now; others will become clearer as any further SEC rulemaking and guidance occurs and as market practices evolve over time. See IX below.

The SEC also formed an Advisory Committee on Small and Emerging Companies to make recommendations regarding capital formation and regulation of these companies. Much of the agenda of the Advisory Committee was overtaken by the JOBS Act, but its efforts may nevertheless result in changes in law and regulations that could affect the subject matter of this outline. In addition, the SEC, as directed by Congress, has formed an Investor Advisory Committee that from time to time makes recommendations in this area that may influence SEC policy.

In another development, active markets have emerged for the resale of shares in non-public companies in order to provide liquidity to holders in the absence of public trading markets. The importance of these resale markets is likely to increase as changes in the threshold for registration under § 12(g) of the Securities Exchange Act of 1934 made by the JOBS Act and reflected in proposed SEC rules will permit companies to remain private longer. These resale transactions raise various issues, such as the basis for their exemption from registration, their impact on the exemption for the original issuer transaction, the extent to which general solicitation affects their exemption and the consequences of the unavailability of information

about the issuer of the securities being resold. For a discussion of private offering exemptions outside the safe harbors, including for resales, see *Law of Private Placement (Non-Public Offerings) Not Entitled to Benefits of Safe Harbors – A Report*, Committee on Federal Regulation of Securities, ABA Business Law Section, 66 Bus Law 85 (Nov. 2010). The resolution of these issues as more attention is paid to these secondary trading markets also could affect the subject matter of this outline.

C. Staff Positions

1. Over the years, the staff of the SEC's Division of Corporation Finance has revisited some of the basic concepts under the Securities Act of 1933 involving the relationship of private and public offerings. In more recent years, the staff has focused on certain issues associated with PIPES (private investment, public-equity) transactions and private equity lines, and on the availability of the benefits of resale registration under Rule 415. The staff has explained some of its positions as resulting from practitioners and their clients becoming too aggressive with respect to issues under §5 of the Securities Act. The staff's positions need to be understood so that transactions can be structured to avoid the pitfalls. To assist this understanding, these positions have become more transparent in recent years as the Commission and the staff have published their interpretations.

2. Dialog between the staff and the private bar and the SEC's adoption of Rule 155 and issuance of Commission guidance described below resolved some of the issues that have arisen over the years and clarified others. However, some issues remain outstanding and new ones have arisen. This author's article *"Basic Securities Act Concepts Revisited,"* INSIGHTS, May 1995 at p. 5, discussed some of these issues and the policy implications of the staff's approach to them, as they existed at that time.

3. While the staff is continuing to apply its positions, they have from time to time shown greater flexibility in their application and have taken into account some of the policy considerations and practicalities. The extent to which the staff is prepared to do so seems to ebb and flow, influenced in part by the perceived aggressiveness of the private sector and the shifting emphasis between investor protection and capital formation. As noted above and discussed below, the staff has focused on what they view as problematic PIPES and private equity line practices.

4. The JOBS Act and SEC rulemaking under it create a new set of issues that will require clarification and guidance. The SEC staff has begun to rethink some of the concepts in view of the JOBS Act changes. This outline will attempt to identify some of these issues and suggest responses to them.

D. Merging of the Public/Private Distinction

1. The staff's positions on the integration of public and private offerings are attributable in part to the strains placed upon basic Securities Act concepts by the blurring of distinctions between public and private offerings. This blurring will only increase as a result of certain provisions of the JOBS Act. Issuers have been seeking the flexibility of quick access to

the public or private markets, both domestically and offshore, based on which is available and which will produce the most favorable terms. They file shelf registration statements to cover public sales, which may be to one or a few investors, while also doing private placements, which might be to a large number of eligible investors. Investment bankers may act as underwriters or placement agents, often interchangeably. At the same time, there has been a trend toward combining the speed and certainty of a private placement with the pricing benefits that flow from the greater liquidity of having registered securities. This has been accomplished through techniques such as PIPES, A/B Exchange Offers and private equity lines, as well as through the use of Rule 144A offerings. Public offerings also have evolved to obtain some of the benefits of private transactions through such techniques as registered direct offerings and confidentially marketed public offerings. We are likely to see Rule 506 exempt offerings conducted like public offerings and increased private solicitation of institutional accredited investors in connection with public offerings, with perhaps the flexibility to complete the offering either publicly or privately or both.

2. As the market for PIPES and private equity lines has become more developed, institutional investors in those markets have become more creative in efforts to achieve liquidity, reduce risks and increase returns. These financing alternatives have become an increasingly important source of capital for small and mid-cap companies, even taking into account the post-2008 disruption in the financial markets. The JOBS Act may create other financing routes that can be considered by these companies as alternative methods of financing.

3. One consequence of the focus on the public/private offering issues has been an expanded use by eligible issuers of shelf registrations, particularly a universal shelf. Securities Offering Reform referred to below accelerated this trend.

4. Another development has been the shortening of holding periods under Rule 144, especially for non-affiliates. This shortening, and the resulting increased liquidity, has taken some of the pressure off the resale registration component, although registration typically is still required in PIPES. On the other hand, as noted above, the increase in the § 12(g) registration threshold may increase pressures for resale liquidity.

E. The Historic Influence of Roll-Ups

On a historic basis, the staff initially had to confront the issue of roll-ups, as mandated by Congress, but subject to the constraint that the roll-up rules apply only to public offerings. Roll-up transactions frequently took place in the context of a reorganization or conversion of private partnerships coupled with an initial public offering of a real estate investment trust. In order to bring these “private” roll-ups under the roll-up rules, the staff sought to integrate the “private” roll-up with the REIT public offering. Having taken this position in the case of roll-ups, as a matter of consistency the staff carried over the same restrictive interpretations to more traditional transactions.

F. Commission Past Responses

1. In 1996, the Commission issued a concept release on "Securities Act Concepts and Their Effects on Capital Formation," Release No. 33-7314 (July 25, 1996), in which it asked for comment on what changes should be made to reform the current regulation of the capital formation process, including addressing problems of integrating public and private offerings. This followed a report of the Commission's Advisory Committee on the Capital Formation and Regulatory Process delivered in July 1996, which recommended adoption of a "company registration" system, and a report of an SEC internal Task Force on Disclosure Simplification issued in March 1996.

2. The American Bar Association's Committee on Federal Regulation of Securities responded by letter dated December 11, 1996 commenting on the various proposals, endorsing some of them and proposing a model for a long-term solution. This model reflected many of the concepts suggested by Linda C. Quinn, then Director of the SEC's Division of Corporation Finance, in a speech to the ABA Committee in November 1995. The ABA Committee updated its reform proposal in a letter dated August 22, 2001 to then Director of the Division of Corporation Finance, David B.H. Martin, and then in its comment letter on the Securities Offering Reform proposal referred to below.

3. Then SEC Chairman Arthur Levitt, in a January 1997 speech entitled "Corporate Finance in the Information Age," recognized the problems created by these "metaphysics" and the need to begin to address them, including possibly removing some of the barriers between private and public offerings.

4. On November 3, 1998, the Commission issued a release that proposed far-reaching changes to the securities registration system and sought to address the problems created by the "metaphysics." Release No. 33-7606 (Nov. 3, 1998) (the "Comprehensive Revision Release"). See this author's article "*The SEC Integration Proposals,*" INSIGHTS, January 1999 at p. 23. Because of the controversy over the proposed changes to the securities registration system, many of the proposals in the Comprehensive Revision Release were not pursued. Although not adopted, these proposals may be relevant in understanding the staff's positions, particularly where the Release sought to clarify the existing staff positions on these issues.

5. The integration proposals in the Comprehensive Revision Release were widely applauded. They were eventually adopted in scaled-back form as Rule 155 on January 26, 2001 in Release No. 33-7943 (the "2001 Release"). See this author's article, "*Understanding the New Integration Safe Harbors under Rule 155,*" INSIGHTS, April 2001 at p. 2.

6. The underlying mission of the Comprehensive Revision Release of streamlining the securities registration process has been accomplished by Securities Offering Reform, Release No. 33-8591 (July 19, 2005). However, this initiative purposefully did not address problems with private offerings or integration of public and private offerings.

7. In December 2004, the Commission established an Advisory Committee on Smaller Public Companies, which issued its report with recommendations, including with respect to capital formation issues, in April 2006. The Committee identified problems in the PIPES transaction area but did not make specific recommendations.

8. In August 2007, in the Proposing Release for revision of Regulation D, Release No. 33-8828 (Aug. 3, 2007) (the "Reg. D Proposing Release"), the Commission provided helpful interpretive guidance on certain public/private offering integration issues. This guidance remains relevant and is discussed below.

9. The Commission had begun, before enactment of the JOBS Act, to explore modernizing the regulation of private and other exempt offerings and addressing more fully the public/private offering issues. These efforts are likely to take on more urgency as issues created by the JOBS Act arise. See IX below.

II. SUMMARY OF BASIC CONCEPTS

The following is a brief review of some of the basic Securities Act concepts involved in the staff's analysis of public/private integration issues.

A. Offer and Sale

1. Under §2(a)(3), "offer" is defined broadly to encompass not only the common law concept of an offer sufficient to form a contract upon acceptance but any attempt to dispose of a security. The meaning of the term, which triggers §5(c) of the Securities Act, remains elusive. Some relief is provided by §2(a)(3) which excludes from the definition of "offer" a right to acquire a security which is not exercisable until some future date, as well as preliminary negotiations and agreements with underwriters in privity of contract with the issuer.

2. The SEC has adopted rules excluding certain communications and activities from the term "offer" and the related concept "prospectus." *See, e.g.*, Rules 134 through 139; *see also* Rule 255 under Regulation A (as amended to implement the JOBS Act). The SEC also has provided interpretive guidance regarding certain activities that do not constitute "offers". See II.E.8 below. The JOBS Act excludes research reports by broker-dealers, including underwriters of a public offering, from being offers. Certain promotional activity that does not reference capital raising also might not be an "offer".

3. The term "sale" presents less difficulty and includes every contract of sale or disposition of a security for value. Securities Offering Reform in particular focused on the importance of the concept of "contract of sale." See Rule 159.

4. The terms are important because of the staff's strongly-held traditional view that a transaction commenced as a private offering cannot be completed as a registered sale; rather both the offer and sale must be either private or registered. This position is confirmed by the Commission in note 122 of the Reg. D Proposing Release. See also Division of Corporation Finance Compliance and Disclosure Interpretations ("C&DI") (available at

www.sec.gov/divisions/corpfin/cfguidance.shtml) §§ 139.29, 139.30 and 239.13 discussed in VII.B below.

B. Underwriter

1. The term underwriter under §2(a)(11) means not only the traditional market professional but also others who purchase from the issuer or a controlling person with a view to, or assist in connection with, a distribution. Its purpose is to deny the §4(a)(1) exemption and thus impose the registration requirements on not only the issuer but also on anyone acting as a conduit for the issuer or its affiliates. Over the years, the staff has sought to characterize various parties as underwriters so as to extend the protection of registration to investors who purchase from these parties. See *Zacharias v. SEC*, 569 F3d 458 (DC Cir. 2009).

2. Another consequence of characterizing a party as an underwriter is to convert that party's resale into a primary offering by the issuer. One of the results of conversion to a primary offering is to change the standard for availability of Rule 415 allowing delayed and continuous offerings and the ability to use Form S-3 short-form registration. In addition, the exemption for the original offering may be called into question.

3. Prior to 1983, the staff treated the purchaser of a large block of a public offering (typically in excess of 10%) as a presumptive underwriter, restricting its ability to resell freely the purchased securities. In *American Council of Life Insurance* (avail. June 10, 1983), the staff put to rest the presumptive underwriter doctrine, at least in the case of an institutional investor purchasing in the ordinary course of its investment activities without arrangements for a redistribution. The staff has since confirmed that the presumptive underwriter doctrine will not be applied to the initial purchasers in a registered offering regardless of the percentage of the offering purchased or the nature of the purchaser (assuming it is not a market professional, *i.e.*, a broker-dealer). However, as discussed below, this concept has reappeared in another guise in the case of certain PIPE transactions.

4. A similar liberalization of the underwriter concept is reflected in the A/B exchange offer line of no-action letters beginning with *Exxon Capital Holding Corp.* (avail. May 13, 1988). These letters permit certain privately placed securities to be exchanged for similar registered securities without the holders being classified as underwriters. However, this does not apply to market professionals, which continue to be considered statutory underwriters. *See Shearman & Sterling* (avail. July 2, 1993).

C. Integration

1. The concept of integration of offerings was developed to prevent circumvention of the registration requirements through the separation of a single non-exempt offering into several exempt offerings. The several offerings, when integrated, are treated as a single offering to determine whether an exemption is available. Integration historically has been applied to test two or more otherwise exempt offerings. Today, the concept also is being applied to test exempt private offerings with registered offerings to determine whether there is gun-jumping or impermissible general solicitation, as well as to determine whether securities issuable

on conversion or exercise may be registered. See the discussion in IX below regarding questions raised by the JOBS Act.

2. In 1962, in Release No. 33-4552, the SEC announced a five factor test to determine whether separate offerings should be integrated. The five factors are: (1) whether the offerings are part of a single plan of financing; (2) whether the offerings involve issuance of the same class of security; (3) whether the offerings are made at or about the same time; (4) whether the same type of consideration is to be received; and (5) whether the offerings are for the same general purpose. These are reflected in the note to Rule 502(a) of Regulation D. The SEC has indicated that there are circumstances in which offerings by affiliated issuers can be integrated. *See Intuit Telecom Inc.* (avail. Jan. 26, 2009) and C&DI § 256.02. The five factor test has not brought certainty to the area because its application is subjective and the staff has not provided definitive guidance as to what weight to give to the various factors or indeed how many of them have to be met. *See Sonnenblick, Parker & Selvers* (avail. Jan. 1, 1986). An ABA Task Force proposed an integration safe harbor rule to provide increased certainty, but the suggested rule has not been adopted by the Commission. *See* ABA Task Force Report on *"Integration of Securities Offerings,"* 41 Bus. Law. 595 (1986).

3. In order to provide some certainty, the SEC has adopted integration safe harbors under certain of the specific exemptions. These include (i) Rule 502(a) under Regulation D excluding from integration offerings more than six months before or six months after the Regulation D offering (this was proposed to be shortened to 90 days but that proposal has not been adopted); (ii) Rule 147(b)(2) establishing a similar six-month safe harbor for intrastate offerings; (iii) Rule 701(f) separating out employee benefit plans; (iv) Rule 251(c) under Regulation A providing a safe harbor for all prior offers and sales and for specified subsequent offerings, including registered offerings and offerings more than six months after completion of the Regulation A offering; (v) Rule 144A(e) for resales to qualified institutional buyers; and (vi) the position reflected in Rule 500(g) (formerly Preliminary Note 7 to Regulation D), as well as Release No. 33-6863 (Apr. 24, 1990), that offshore sales under Regulation S will generally not be integrated with domestic offerings.

4. Rule 152, adopted in 1935 in Release No. 33-305, is a safe harbor for issuers undertaking a public offering or filing a registration statement after conducting a private offering. As interpreted by the staff, a completed private offering will not be integrated with a subsequently commenced public offering. *See Verticom, Inc.* (avail. Feb. 12, 1986), which reversed *LaserFax, Inc.* (avail. Sept. 16, 1985); *see also Vulture Petroleum Corporation* (avail. Feb. 2, 1987) and *Quad City Holdings, Inc.* (avail. April 8, 1993). This position has been confirmed by the Commission in the Reg. D Proposing Release. Note that Rule 152 provides protection for private offerings under §4(a)(2) and the Rule 506 safe harbor under it but not for the §3(b) exemptions under Rules 504 or 505 or the North American Securities Administrators Model Accredited Investor Exemption, such as the one adopted in California and recognized by the SEC in Rule 1001 under Regulation CE (the "State Accredited Investor Exemption").

5. *Black Box Incorporated* (avail. June 26, 1990), as amplified by *Squadron, Ellenoff, Pleasant & Leher* (avail. Feb. 28, 1992), addresses the availability of Rule 152 and

other integration issues in the context of related private and public offerings. This has been augmented by the Commission's guidance in the Reg. D Proposing Release discussed below. In point 4 of the *Black Box* letter, the staff made clear that the private offering had to be completed before filing of the registration statement for Rule 152 to apply and that the offering would be considered completed if there are binding commitments subject only to conditions outside the investor's control. The SEC staff indicated that renegotiation of terms after the registration statement is filed could make Rule 152 inapplicable. Abandonment of a private offering could also constitute its completion. *See also, United States Enrichment Corporation* (avail. May 13, 1998). See V.C.4 for the staff's interpretation of "complete" for purposes of private equity lines.

6. The *Black Box* interpretive position has been recognized judicially in *Anegada Master Fund, Ltd. v. PXRE Group LTD.*, 680 F. Supp. 616 (SDNY 2010), in which the court recognized the "nature and number of offerees" as a sixth factor based on the SEC's guidance.

7. The SEC adopted Rule 155 in the 2001 Release. Rule 155 provides two safe harbors from integration, one for undertaking a registered public offering after abandoning a private offering, and the other for undertaking a private offering after an abandoned registered public offering. See VIII below.

8. New § 4(a)(6) of the Securities Act added by the JOBS Act to permit creation of a "crowdfunding" exemption seems to contemplate in subsection (g) that a crowdfunding offering will not affect use of other exemptions. However, general solicitation that may be permitted for a concurrent Rule 506 offering could be inconsistent with the limitations on advertising contemplated by § 4(a)(6) for a crowdfunding offering.

D. Gun-Jumping

1. Gun-jumping is a concept that applies to activities before or during the registration process that violate § 5 of the Securities Act. Typically, gun-jumping has been applied to impermissible publicity during the pre-filing or waiting periods. However, it is also used to describe any offer prior to the filing of the registration statement that violates §5(c) of the Securities Act.

2. It has been the staff's position that securities offered to investors based on the private offering exemption cannot subsequently be registered for sale to those investors since, viewed as a single transaction, the offer before filing of the registration statement would involve gun-jumping. See C&DI § 139.09. Notwithstanding that the language of Rule 152 appears to permit converting a private offering into a registered offering, the staff's view is that Rule 152 does not apply to an offer and sale in the same transaction.

3. The JOBS Act adds a new subsection (d) to § 5 of the Securities Act to provide that test-the-waters oral or written communications by or on behalf of "emerging growth companies" to qualified institutional buyers and institutional accredited investors before or after the filing of a registration statement are permissible and therefore do not constitute gun-jumping. As noted above, the JOBS Act also permits underwriters to issue research reports.

E. General Solicitation

1. A fundamental basis for the private offering exemption, in the historic view of the Commission, is the absence of general solicitation of investors. This principle took on increased importance with the adoption of Regulation D, which eliminated offeree qualification requirements. Rule 502(c) of Regulation D prohibited general solicitation in Rule 505 and Rule 506 offerings and, after September 23, 2013, prohibits it in Rule 505 and Rule 506(b) offerings. The Commission requested comment in Release No. 33-7185 (June 27, 1995) and again in Release No. 33-7314 (July 25, 1996) and in the Reg. D Proposing Release as to whether this prohibition of general solicitation should be eliminated or modified. The Commission proposed a step to soften this prohibition by proposing Rule 157, which would have permitted limited advertising to a defined category of "super-accredited investors." This rule was not adopted.

2. The JOBS Act permits general solicitation in Rule 506 offerings by directing the SEC to amend Rule 506 to eliminate the prohibition on general solicitation if all purchasers are accredited investors (which is defined in Rule 501(a) as anyone who is or who the issuer reasonably believes is an accredited investor). It requires that an issuer take reasonable steps to verify that purchasers are accredited investors using methods prescribed by the SEC. The JOBS Act also adds § 4(b) to the Securities Act which provides that a Rule 506 offering shall not be a public offering as a result of general solicitation. In addition, the JOBS Act directs the SEC to permit general solicitation for Rule 144A offerings by eliminating the prohibition on offers to non-QIBs. The SEC, after proposing amendments to Rule 506 and Rule 144A to implement these provisions of the JOBS Act in Release No. 33-9354 (Aug. 29, 2012) (the "Rule 506 Proposing Release"), has adopted amendments along the lines proposed that became effective September 23, 2013. The amendment of Rule 506 retains the existing Rule 506 exemption as Rule 506(b) and adds a new exemption as Rule 506(c) under which there could be general solicitation if all purchasers are accredited investors and the issuer takes reasonable steps to verify that purchasers are accredited investors. See Release No. 33-9415, *Eliminating the Prohibition Against General Solicitation and General Advertising in Rule 506 and Rule 144A Offerings* (July 10, 2013) (the "Rule 506 Adopting Release"). What are reasonable steps to verify will depend upon the particular facts and circumstances, although the SEC provided non-exclusive safe harbors for verifying the status of natural persons. *See* C&DI §§ 260.35-260.38, in which the SEC makes clear that the safe harbors must be strictly complied with but emphasizes that the principles-based approach based on the particular facts and circumstances may be relied upon, especially applying principles derived from the safe harbors. The SEC also added "bad actor" provisions to Rule 506 in Release No. 33-9414, *Disqualification of Felons and Other "Bad Actors" from Rule 506 Offerings* (July 10, 2013) as directed by the Dodd-Frank Act. *See* C&DI §§ 260.14-260.32. At the same time it adopted these changes, the SEC proposed additional changes to enable it to obtain information to monitor developments in the new exempt offering market in the interest of investor protection. See Release No. 33-9416 (July 10, 2013) (the "2013 Rule 506 Proposing Release"). See this author's article *"General Solicitation: What Congress Giveth, the SEC Proposes to Taketh Away"* INSIGHTS, August 2013 at p. 15.

3. One partial step in eliminating the general solicitation prohibition was taken in 1996 with the adoption of Rule 1001 exempting offerings that complied with California's State

Accredited Investor Exemption, but only for offerings up to $5 million. The Commission indicated that it would extend the exemption to other states that adopted requirements similar to those of California but to date the exemption has not been extended. General solicitation can also occur in a Rule 504 offering, provided that certain state blue sky law requirements are met.

4. The Commission had taken the position that the mere filing of a registration statement for a specific offering, even without offering activity (*i.e.*, a quiet filing), constitutes general solicitation of the security that is registered. Letter dated March 23, 1984 from John J. Huber, Director of the Division of Corporation Finance, to Michael Bradfield, General Counsel of the Board of Governors of the Federal Reserve System. *See also* SEC Litigation Release No. 10241 (December 19, 1983) regarding Traiger Energy Investments and *Circle Creek AquaCulture V, L.P.* (Mar. 26, 1993). Consequently, the exemption for a private offering of the same or a similar security undertaken during the pendency of a filed registration would not have been available as a result of general solicitation if the private offering were integrated with the registered offering. To the extent this remains a concern, emerging growth companies have the ability under the JOBS Act to submit their registrations statements to the SEC for review confidentially, which may negate the general solicitation.

5. The *Black Box* letter (point 3) carved out on policy grounds a limited exception for a private offering during the pendency of a registration statement to "qualified institutional buyers" and a few other institutional accredited investors. In the *Squadron, Ellenoff* letter the staff indicated that this exception is to be narrowly construed, stating that it is limited to qualified institutional buyers and no more than two or three large institutional accredited investors.

6. There were questions regarding the scope of the *Black Box* exception. For example, did it apply to "underwritten" 144A offerings taking place contemporaneously with a registered offering? The SEC staff indicated that it did apply, pointing to the non-fungibility requirement of Rule 144A. Did it apply to private offerings involving management along with QIBs? The prevailing view was that it did apply pursuant to the so-called "Macy position" (see C&DI § 139.25). Another question, discussed below under V.B, is whether additional tranches of similar securities can be sold in Rule 144A offerings to QIBs while the first tranches are being registered either as part of an A/B Exchange Offer or for resale in a PIPE transaction? Some of these questions have been resolved with the elimination of the prohibition on general solicitation in a Rule 144A offering.

7. In the Reg. D Proposing Release, the SEC put to rest the "presumptive general solicitation" concept reflected in the *Bradfield* letter, and instead said that whether or not there was general solicitation of investors after a registration statement had been filed was a facts and circumstances determination that, unlike *Black Box*, did not turn on the nature of the investors. See this author's commentary *"SEC Provides Private/Public Offering Integration Guidance,"* INSIGHTS, September 2007 at p. 19. The relevant analysis is whether the investor was obtained through a general solicitation, such as because of the filing or public offering marketing. On the other hand, if the company can demonstrate that the investor was reached through other means, such as a pre-existing, substantive relationship or direct contact outside the public offering

process, a private offering exemption could be available. This would be easier to show if there was a quiet filing. In addition, as noted above, emerging growth companies can confidentially submit the registration statement. The Commission's guidance provides increased flexibility for companies in registration to raise needed capital privately. See also C&DI § 139.25 in which the staff confirms that the five-factor integration test does not have to be satisfied in order to utilize the Commission's guidance on concurrent private and public offerings. On the other hand, if a private offering would not be integrated with a public offering under the five-factor test, it would not be necessary to rely on this guidance. With the amendment to Rule 506 to permit general solicitation if all purchasers are accredited investors and the issuer takes reasonable verification steps, the facts and circumstance analysis under the Commission's guidance would be unnecessary for these offerings. On the other hand, the guidance can take on even more significance in other contexts. The SEC Chairman in a letter to Congressman Issa, *avail. http://www.wowlw.com/White%20Response%20to%20McHenry%20Letter.pdf*, acknowledged that the guidance could apply outside the IPO context.

8. What constitutes general solicitation in an elusive concept. Although the JOBS Act changes resulting in Rule 506(c) did not affect what is general solicitation, and any activities that were permissible in a Rule 506 offering before September 23, 2013 should still be permissible under Rule 506(b) subsequently (See Rule 502(c)), the adoption of Rule 506(c) establishing a means of engaging in general solicitation while having an exempt offering has caused renewed focus on what activities can be undertaken without being general solicitation and triggering the requirements of Rule 506(c). The SEC has provided guidance regarding certain activities that do not constitute "offers" and other activities that do not involve general solicitation, including as a result of a pre-existing, substantive relationship with the offeree. See C&DI §§ 256.23 – 256.33 and *Citizen VC, Inc.* (Aug. 6, 2015). See also this author's article *"SEC Guidance on General Solicitation Provides New Opportunities,"* INSIGHTS, September 2015 (to be published). A detailed discussion of general solicitation is beyond the scope of this outline.

III. CONVERTIBLE SECURITIES AND WARRANTS

A. Registering Issuance of Underlying Securities

1. The staff's position is that privately placed convertible securities and warrants represent an ongoing private offering of the underlying securities, at least if they are then currently convertible or exercisable, and therefore the issuance of the underlying securities cannot be registered. Rather, an exemption would have to be found for the issuance of the underlying securities on conversion (*e.g.*, §3(a)(9), if available) or exercise and those securities could be registered for resale. The staff has indicated that a shelf resale registration of the underlying securities would not prevent those securities from being issued pursuant to a private offering exemption upon conversion or exercise.

2. On the other hand, if the convertible securities or warrants are not convertible or exercisable until some future date, there would be no "offer" under §2(a)(3) and consequently

a registration statement covering issuance of the underlying securities could be filed before the convertible securities or warrants become convertible or exercisable.

3. The question exists as to how long conversion or exercisability must be deferred for there not to be an "offer." The staff has not settled on the period but requires that there be a significant period prior to exercisability and points to its longstanding position taken in the registration process that a one-year non-exercisability period is necessary to avoid the need to register the underlying securities upon a public offering of convertible securities or warrants. See C&DI § 139.01. Some counsel have been comfortable with a shorter period.

4. The staff has indicated that the convertible securities or warrants could themselves be registered for resale, in which case the issuance of the underlying securities upon conversion or exercise could also be registered, although not for issuance to the private purchaser of the convertible securities or warrants.

5. Although the logic of the staff's position would extend to employee stock options, the staff recognizes that the practice has been to include in the Form S-8 registration the shares underlying employee stock options that were granted and may have become exercisable prior to filing. This practice was confirmed by the staff in the Division of Corporation Finance Manual of Publicly-Available Telephone Interpretations – July, 1997, Securities Act Forms Item 61 and now appears in C&DI § 239.15. The staff has traditionally been more accommodating regarding employee benefit plans since they present fewer concerns than capital raising activity.

B. Integrating Convertible Securities with a Registered Offering

1. The question arose whether a separate public offering of the same class of securities as were issuable upon conversion or exercise of privately placed convertible securities or warrants would be integrated with, and therefore defeat the exemption for, that private placement since there was a continuing offering of the underlying security. For example, this question was raised by the staff in the context of an initial public offering of common stock following the private offering of convertible preferred stock, a typical form of investment in venture-capital backed companies. The staff has since indicated that the integration analysis should be based on the status at the time of the private placement of the convertible securities and warrants. If that placement was completed before the filing of the registration statement, Rule 152 could be applied to avoid integration with the public offering. This position was reflected in the Comprehensive Revision Release proposal.

2. Sometimes warrants are issued for nominal consideration in order to avoid later integration with a public offering. The staff's position is that warrants issued for nominal consideration are not treated as issued for this purpose and therefore are not entitled to the benefit of being tested at the time of their issue for purposes of the Rule 152 integration analysis. If the warrants are being issued as part of a larger transaction (e.g., convertible securities with warrants), it seems appropriate to take into account the entire transaction to see if more than just nominal consideration was paid. The issuance of warrants for nominal consideration, while not treated as issued for purpose of the Rule 152 analysis, could still raise gun-jumping issues. See V.E below.

IV. PRIVATE FORMATION TRANSACTIONS

1. The staff has confirmed that restructuring or formation transactions outside the roll-up context will not be integrated with the initial public offering which they were undertaken to facilitate. This position would have been partially codified by the Comprehensive Revision Release proposal. Examples of such transactions are the combination of several private companies to form the entity that goes public, the issuance of common stock to founders followed by an initial public offering, or the conversion of outstanding founder debt to common stock in connection with the initial public offering.

2. The staff has emphasized, however, that the restructuring or formation transactions in and of themselves have to comply with the Securities Act (*e.g.*, the combination of several entities with outside investors may have to be tested for an exemption on an integrated basis applying the five factor integration test).

V. PRIVATE TO PUBLIC OFFERINGS

A. A/B Exchange Offers

1. The *Exxon Capital* line of letters has created a procedure under which securities are privately placed and then promptly exchanged for similar securities which have been registered and therefore are freely resalable. *See Exxon Capital Holding Corp.* (avail. May 13, 1988), *Morgan Stanley & Co. Incorporated* (avail. June 5, 1991), *Mary Kay Cosmetics, Inc.* (avail. June 5, 1991), *Warnaco Inc.* (avail. Oct. 11, 1991), *Epic Properties, Inc.* (avail. Oct. 21, 1991), *Vitro, S.A.* (avail. Nov. 19, 1991), *Corimon C.A.S.A.C.A.* (avail. Mar. 22, 1993), *K-III Communications Corporation* (avail. May 14, 1993) and *Brown & Wood LLP* (avail. Feb. 7, 1997). However, this procedure is only available for nonconvertible debt securities, certain types of straight preferred stock and initial public offerings of common stock of foreign issuers, and the staff has indicated that it is not prepared to extend its use. The Securities Offering Reform Rules do not address A/B exchange offers and do not give credit for them in assessing an issuer's status as a debt-only "well-known seasoned issuer." On the other hand, the SEC staff has indicated that the A/B exchange offer does not double count for purposes of determining the amount of debt issued to test the issuer's status as an emerging growth company.

2. Typically, the issuer will place the securities privately to institutional investors or sell them pursuant to the private offering exemption to investment bankers who resell them to qualified institutional buyers under Rule 144A, to accredited investors under Regulation D and offshore pursuant to Regulation S. Upon the registered exchange offer the holders get freely tradable securities if they are not affiliated with the issuer, acquired the original securities in the ordinary course of business and do not have any arrangement for the distribution of the exchange securities.

3. In the *Shearman & Sterling* letter, the SEC placed special requirements on broker-dealers participating in the exchange offer.

4. The availability of the exemption in an A/B exchange offer utilizing Rule 144A in contemplation of a registered exchange offer was at issue, based on its being a "plan or scheme to evade" registration under Note 3 to Rule 144A, in the *HealthSouth Securities Litigation*. The SEC filed an amicus letter dated November 28, 2006 supporting the availability of the exemption. This letter provides helpful analysis of the SEC's views regarding the A/B exchange offer transaction and related concepts.

B. PIPES

1. PIPE transactions involve a procedure in which investors agree to purchase the securities in a private offering on the understanding that a registration statement covering the resale of the securities will be filed and become effective. PIPES can be viewed as an evolution of registration rights. These rights began as the grant of contractual demand and piggyback registration rights; then there was a contractual covenant to provide a shelf registration within a prescribed period, often coupled with a penalty for noncompliance in the form of an increased rate of interest or dividends, adjustment of conversion price or even redemption; this was followed by having as a condition of the closing that the registration statement be filed; and in its ultimate form the closing condition could require that the shelf resale registration statement be effective. PIPES can be traditional or structured. In a traditional PIPE, the investor agrees to buy the security at a fixed price or a fixed conversion ratio. In a structured PIPE, a convertible security typically is used and the conversion price is adjusted based on a formula usually tied to the market price of the underlying common stock during a period prior to the conversion. Warrants may also be involved.

2. The staff has confirmed that PIPE transactions are permissible if done correctly and the Comprehensive Revision Release reflected this position. See also, the Division of Corporation Finance Manual of Publicly Available Telephone Interpretations Supplement – March 1999 ("Telephone Interpretations Supplement"), #3S(b) and C&DI § 139.11. To be done correctly, the private offering must be completed before the resale registration statement is filed so that Rule 152 is available. The *Black Box* letter (points 1 and 2) makes it clear that the offering is completed if commitments are in place from all investors subject only to conditions outside their control so that there is no further investment decision. Examples of acceptable conditions are the filing or effectiveness of a resale registration statement or receipt of regulatory approvals. A no material adverse change condition should be an acceptable condition since there is an objective standard but a diligence out would not be acceptable. See V.C below. In addition, the staff has indicated that a closing condition based on the market price of the issuer's securities would not be acceptable because the investors would not be at risk and therefore the private offering would not have been completed at the time of filing. On the other hand, the staff has indicated that convertible securities with the conversion price tied to the market price of the underlying common stock (*e.g.*, formula preferred) would not prevent the investor from being at risk. The staff also has confirmed that the use of a market price formula and collars in merger and acquisition transactions is permissible since these do not involve capital raising and therefore are not subject to the same abuse. The staff has been rethinking whether a variable price or market price condition will prevent having a completed private offering or whether it should just relate to the status of the investor as an underwriter, but it continues to be the position that

market risk is a requirement for completion of the offering for purposes of Rule 152. The staff also requires that the closing take place promptly after the resale registration becomes effective so that it is a valid secondary offering and not a delayed primary offering. See V.C below. The staff's position on PIPE transactions continues to evolve and new issues surface. See V.D below.

3. If not done correctly, you have a "burst PIPE." See C&DI § 139.11. Renegotiation of terms, at least if they are material, after the registration statement is filed is not permissible. In addition, if the issuer obtains additional commitments from private investors after the filing, these post-filing offers would be considered part of the same offering, and Rule 152 would not be available. Since filing the registration statement is considered by the staff to be general solicitation, there would be no private offering exemption for the subsequent commitments which, in turn, would defeat the exemption for the prior commitments because of integration. The Commission guidance in the Reg. D Proposing Release is unlikely to be helpful here because the post-filing offers could be viewed as part of the same offering as opposed to a separate private offering. See C&DI § 139.08.

4. It is unclear whether the ability to engage in general solicitation under Rule 506(c) will change the PIPE analysis when Rule 152 is not available because of the staff's position that an offering commenced as a private offering cannot be completed as a registered offering. Therefore, reliance on Rule 152 is advisable until there is further clarification. See IX below.

5. Shelf registration of PIPE shares for resale from time to time is dependent upon the availability of Rule 415(a)(1)(i). Recently, the staff has questioned the availability of this rule for delayed or continuous secondary offerings of securities issued in PIPE transactions by issuers that are not primary S-3 eligible when the amount being registered is disproportionately large in relation to the issuer's capitalization, sometimes characterizing the investors as affiliates and the offering as a primary offering. If the availability of Form S-3 for a primary offering is based on Instruction I.B.6 for limited primary offerings by issuers who do not meet the $75 million float test, the portion of the resale offering characterized as a primary offering most likely would have to satisfy the one-third market value cap taking into account under the Instruction prior offerings in the prior 12 months. The consequences for an issuer not eligible to use Form S-3 for a primary offering if the PIPE resale is found to be a primary offering in disguise are that the securities would have to be registered on Form S-1 for a fixed price offering, common shares underlying convertible securities and warrants can only be registered on conversion or exercise, and the selling shareholders would have to be named as underwriters. The staff sometimes refers to Telephone Interpretation, Rule 415, Item 29, which provides that a purported secondary offering may, in some circumstances, really be a primary offering and the selling shareholders actually underwriters selling on behalf of the issuer. Relevant factors include the nature of the securities being registered, whether they are listed on an exchange with substantive standards, how long the shares have been held, the circumstances under which the shares were acquired, the relationship between the selling shareholder and the issuer, the amount of securities involved, the nature of the seller and whether it is in the business of underwriting securities, and whether it appears the seller is acting as a conduit for the issuer.

The SEC recently provided useful guidance, but how these factors will be applied to convert a secondary offering of PIPE shares into an ineligible primary offering is still being developed on a case by case basis, thus creating uncertainty for these types of financings. Depending on the particular circumstances, capping the percentage of shares registered at one-third of the public float may permit the use of Rule 415. The problem is most acute when convertible securities or warrants with variable conversion or exercise prices are involved because of the large number of shares sought to be registered to cover a potential decline in price. The staff has indicted that ownership caps often included in PIPE documentation (but typically waivable on not less than 60 days' notice by the investor) will be disregarded in determining whether the investor is an affiliate. An area of continuing uncertainty is the status of shares not included in the registration because they exceed the cap on the number that can be registered. Alternatives for dealing with those shares range from being able to register additional tranches on Form S-3 in the future, being able to use Rule 144 for resales, to not being able to resell the securities at all except as a registered primary offering because of "underwriter" status. The staff is also focusing on adequacy of disclosure to investors, including costs to the issuer, fees paid, relationships with the seller or its affiliates and impact of potential dilution. See the article by this author and William Hicks *"Unblocking Clogged PIPEs: SEC Focuses on Availability of Rule 415,"* INSIGHTS, May 2007 at p. 2.

6. More recently, the staff has informally confirmed that its focus under Rule 415 is more likely to be on "toxic" PIPES and that traditional "non-toxic" PIPES are unlikely to raise issues. This position creates planning opportunities for smaller public companies because, while use of Form S-3 for a registered primary offering under Rule 415 would be limited under Instruction I.B.6. to one-third of the market value cap, a company might be able to do a PIPE with resale registration on Form S-3 without being subject to that limitation.

7. PIPE transactions also can raise accounting issues that need to be considered to avoid the resale registration statement being delayed in becoming effective.

8. The question has arisen regarding tack-on offerings in 144A transactions where an additional tranch of securities is sold. This occurs in two forms. One involves an A/B exchange offer and the other a PIPE transaction. In the A/B exchange offer, there should be no issue in doing the additional offering if it is completed before the filing of the exchange offer registration statement because Rule 152 would apply. There also should be no issue conducting the additional offering following completion of the exchange offer either in reliance on *Black Box*, by waiting 30 days and using the Rule 155 safe harbor or possibly under a five factor integration analysis based on the registered offering being an exchange offer while the 144A offering is capital raising for cash. An issue is whether the additional offering can be done contemporaneously with the registered exchange offer. Many lawyers believe it can be done contemporaneously based upon a *Black Box* or five factor analysis. The principles underlying the Commission guidance in the Reg. D Proposing Release also might be helpful. The ability to have general solicitation in a 144A offering should make reaching this conclusion easier. In the case of a PIPE transaction, the issue is whether the 144A additional offering can be done after filing the resale registration statement for the first tranches or whether it is a "burst PIPE." Many lawyers have gotten comfortable with this offering when limited to QIBs and 2 or 3 large

institutional investors based on a *Black Box* analysis, taking into consideration that the pending registration statement is for resale rather than a primary offering. Again, the principles underlying the Commission guidance in the Reg. D Proposing Release and amendment of Rule 144A to permit general solicitation might be helpful.

9. PIPE transactions also have raised enforcement issues that relate to insider trading, market manipulation, misrepresentation and violation of section 5 through alleged impermissible short selling or other hedging activity. These issues have involved a number of enforcement actions and at least three court proceedings discussed below. *See, e.g., SEC v. Guillaume Pollet,* Civ. Action No. 05 Civ. 1937 (E.D.N.Y. 2005); *SEC v. Hilary L. Shane*, Civ. Action No. 05 Civ. 4772 (S.D.N.Y. 2005); *SEC v. Rhino Advisors and Thomas Badian*, Civ. Action No. 03 Civ. 1310 (RO) (S.D.N.Y. 2003) and Litigation Release No. 18003 (February 27, 2003); *SEC v. Langley Partners, L.P.*, 05 Civ. Action No. 467 and Litigation Release No. 19607 (March 14, 2006); *SEC v. Deephaven Capital Management*, LLC, 06 Civ. Action No. 805 and Litigation Release No. 19683 (May 2, 2006).

10. *Langley Partners* is important, not only because it is alleged to involve insider trading by selling short before announcement of the PIPE transaction, misleading the issuer by representing the investor would not sell the shares in violation of the Securities Act and violating section 5 of the Securities Act by covering the short sales with the PIPE shares, sometimes wash sales and matched orders, but because it suggests that there is a correct way for PIPE investors to hedge their investment risk. *Langley Partners* can be read to validate the "double print" transaction where PIPE shares are sold in the open market and other shares are purchased in the open market to close out the short sale (which should occur only following dissemination of the announcement of the PIPE transaction), so long as the open market purchases are separated from the PIPE share sales. What is necessary for them to be separate depends on the circumstances, including the vitality of the market in relation to the shares involved, the time between the purchase and sale as evidence of being at market risk and the identity of the broker or brokers involved. *See also, SEC v. Edwin Buchanon Lyon, IV, Gryphon Partners, L.P. et al*., 06 Civ. Action No. 14338 and Litigation Release No. 19942 (Dec. 12, 2006), and *In the Matter of Spinner Asset Management, LLC*, Securities Act Release No. 8763 (Dec. 20, 2006), in which the Commission said:

> Many PIPE investors "hedge" their investment by selling short the PIPE issuer's securities before the resale registration statement is declared effective. There is nothing per se illegal about "hedging" a PIPE investment by selling short the issuer's securities. Such short sales do not violate the registration provisions of the Securities Act if, among other things, the investor closes out the short position with shares purchased in the open market. An investor violates Section 5 of the Securities Act, however, when it covers its pre-effective date short position with the actual shares received in the PIPE. This is because shares used to cover a short sale are deemed to have been sold when the short sale was made.

11. The SEC's position that Section 5 is violated by covering the short sale (directly or by replacing the borrowed shares) with the restricted shares purchased in the PIPE,

even after they have been registered for resale, has been challenged in three court cases, each of which held against the SEC. *See SEC v. Mangan*, Civ. Action No. 3:06-CV-531 (WDNC Oct. 24, 2007; *SEC v. Lyon*, 529 F. Supp. 2d 444 (SDNY Jan. 2, 2008); and *SEC v. Berlacher*, No. 07-CV-3800 (EDPA Jan. 23, 2008). In *Lyon*, the only case with a written opinion, the court held that Section 5 was not violated because, in the court's view, securities later used to close a short position are not sold or offered for sale at the time the short sale is made; rather the buyer received unrestricted borrowed shares used to settle the short sale. Although the SEC has not appealed these decisions, it has made clear that it continues to be its position that, in a short sale, the sale of securities for purposes of Section 5 occurs at the time the short position is established, rather than when shares are delivered to close out that short position, or put another way, the delivery of the securities that were restricted to cover the short position relates back to the short sale. *See* Note 90 of Release No. 33-8869 (Dec. 6, 2007) and C&DI § 239.10. In view of the SEC's position, and the possibility that it could take actions to establish that position, market participants and their advisers would be ill-advised to rely on the decisions in connection with short sale activity. Instead, it would be advisable to follow the course the SEC has indicated works, which is the properly executed "double print." See this author's article "*Short Selling and Section 5*," INSIGHTS, March 2009 at p. 10. See also this author's article "*DC Circuit Gets Section 5 Right*," INSIGHTS, October 2009 at p. 32.

12. In structuring PIPE transactions, the parties need to be mindful of shareholder approval requirements under stock exchange rules when 20% or more of the shares are being issued or can potentially be issued other than in a public offering or there is a change of control. See, e.g., Nasdaq Rule 4350. PIPE investors also need to be concerned that in handling a multi-purchaser transaction they are not treated as part of a group triggering potential section 16(b) liability. Compare *Schaffer v. CC Investments*, 2002 WL 31869391 (SDNY 2002) (finding a group) with *Litzler v. CC Investments*, CCH Fed. Sec. Law Rep. ¶ 93,652 (SDNY 2006) (no group exists).

C. Private Equity Lines

1. Another type of transaction that has raised concerns with the staff is a private equity line under which investors agree to buy equity from the company, with the company having the right to draw down on the commitment on a periodic basis after the resale registration statement has been filed or becomes effective. Typically, the share price is at a discount to the market price at the time of the drawdown. These can be thought of as PIPE transactions with deferred takedowns.

2. It is the staff's view that private equity lines, because of their delayed nature and because when the takedown price is based on a formula tied to market price of the security the purchasers would not be at risk, are indirect primary offerings. Accordingly, as a general rule, Form S-3 may be used only if the issuer is eligible to use Form S-3 for primary offerings and the purchasers under the line must be identified as underwriters and are subject to the restrictions applicable to underwriters in a primary offering (*e.g.*, Regulation M). See "Current Issues and Rulemaking Projects Quarterly Update" dated March 31, 2001 of the SEC's Division of Corporation Finance, at §VIII, "Equity Line Financings," which replaced Telephone

Interpretations Supplement, #4S. Equity lines are now addressed in C&DI §§ 139.12 to 139.24. If the issuer is relying on Instruction I.B. 6, the entire amount of the equity line must be used in applying the one-third market value cap.

3. The staff will, however, permit a resale registration form to be used if the following conditions are met: (i) the private transaction must be "completed" before filing the registration statement; (ii) the registration statement must be on the form the company is eligible to use for a primary offering; and (iii) the investor must be identified in the prospectus as an underwriter, as well as a selling security holder.

4. For the transaction to be "complete," the investor must be irrevocably bound to purchase all the securities. This means that only the company may exercise the put subject only to conditions outside the investor's control. This would include "bring downs" of customary representations and warranties and customary material adverse change conditions. However, a "diligence out" will not qualify, nor may the investor have the right to transfer its obligation under the equity line or to acquire additional securities (such as through the exercise of warrants) at the same time or after the issuer exercises the put. Provisions allowing the investor to affect the timing or price or allowing termination of the put are also suspect. Also, the company may not put securities convertible into the common shares being registered because the investor would have a further investment decision whether to convert and purchase the underlying registered shares. If the investor has a right to take interest payment in shares, the transaction may not be considered "complete." The staff's interpretation of "complete" in this context may have relevance for purposes of Rule 152.

5. If these conditions are not met, the resale may not be registered unless the company is eligible to use Form S-3 (or Form F-3) for a primary offering and the prospectus addresses the potential violation of § 5 in connection with the private transaction.

6. The Quarterly Update referred to in C.2 above also addresses the need in private equity line transactions to comply with Regulation M and NASD pre-filing requirements.

7. The SEC staff has been applying the interpretations that allows private equity lines strictly, and questioning variations from those interpretations. For example, the staff has taken the position that an investor cannot have convertible securities or warrants at the same time as it does an equity line, at least if the two transactions are related, because looked at as a whole, the private offering is not "completed" given the additional investment decision that can be made. Thus, the staff has questioned bridge loans closely related to equity lines, at least where the loan was convertible or accompanied by warrants. The staff also has raised questions about the amount of securities being registered being disproportionate to the size of the issuer's capitalization and indicated that a private equity line cannot be done with an affiliate. The staff has provided guidance with respect to the private equity line issues as follows:

- The equity line must be completed when the registration statement is filed and there can be no renegotiation of material terms (such as extending the term of the line).

- The staff position that permits an equity line to be registered as a resale registration so long as the issuer uses a form for which it is eligible for a primary offering is not available if the investor is an affiliate because the offering is then deemed to be a direct primary offering.

- Any caps imposed on the investor's ability to acquire shares will be ignored by the staff in assessing affiliate status.

- The staff will object to the use of escrows for the committed funds.

- In order for the commitment to be complete, any floor or ceiling to the price collar cannot be waived.

- The investor cannot be in a position to reject or delay the issuer's ability to call on the equity line, such as through a diligence provision or a certification requirement.

- The investor's obligation cannot be transferable or assignable.

- The investor cannot have a convertible security or warrants in connection with an equity line because it would then have a further investment decision.

- The equity line cannot be used to effect an initial public offering; rather there must be an existing trading market.

- The investor cannot receive convertible securities or warrants before registration of the equity line.

- There must be adequate disclosure of all fees, side deals and related transaction, as well as the proposed use of proceeds from the line (such as repayment of loans).

- If the amount of securities being registered is substantial in relation to the issuer's public market float the offering will be considered to be in reality an issuer primary offering, with the investor being an "underwriter".

See Keller and Hicks, *"Unblocking Clogged PIPEs: SEC Focuses on Availability of Rule 415,"* INSIGHTS, May 2007 at p.2.

D. Converting to a Public Offering

1. The staff has not permitted a transaction commenced as a private offering to be converted to a registered offering covering the issuance of the securities. They have viewed this as inconsistent with the registration provisions and a violation of §5(c) of the Securities Act. See "Current Issues and Rulemaking Projects" dated November 14, 2000 of the SEC's Division of Corporation Finance at § VIII.A.9 (second paragraph) and C&DI §§ 139.06 and 139.09.

2. However, if the private offering is terminated, the staff has allowed a subsequent registered offering. See point 4 of the *Black Box* letter. Prior to the Comprehensive Revision Release, the staff had not articulated what is necessary for termination of the private offering, but had indicated that private practitioners can make that determination. The traditional five factors of Release No. 33-4552 would be relevant. Although sales to different investors would be helpful, the staff indicated that investors contacted in the private offering are not necessarily foreclosed from participating in the registered offering.

3. Rule 155 establishes a safe harbor for doing a registered offering following an abandoned private offering, but does not address what is required for termination of the private offering for purposes of Rule 152 outside the safe harbor. See VIII.B below.

4. The ability to test-the-waters with QIBs and institutional accredited investors, as provided in the JOBS Act, may result in a different analysis that permits discussing a private offering with these investors and then deciding whether to complete the private offering or abandon it and proceed with the public offering. Moreover, with general solicitation being permitted for a Rule 506(c) offering, it may be possible to complete the private offering and include these investors in a public offering. See IX.B below.

5. In *United States Enrichment Corporation* (avail. May 13, 1998) the question was posed whether a company could simultaneously pursue a private sale of the company and an initial public offering, with a decision which way to go being made before filing the registration statement. The facts were unique, involving the privatization of a U.S. government corporation, but the staff confirmed that the acquisition process could be terminated before filing the registration statement and would not be integrated with the initial public offering. This is a fairly obvious application of Rule 152 and *Black Box* point 4. A more interesting question would have been whether the efforts to privately sell the company could have continued during the pendency of the registration statement. The answer should be that it could have continued based on a traditional five factor analysis since the private sale efforts were not for capital raising purposes but rather were to dispose of the entire company. The analysis might be different if it were a disposition of only a partial interest in the company, particularly a minority interest. However, if the private offering is structured as a Rule 506 offering with sales solely to accredited investors, there should be no problem with proceeding once general solicitation is permitted. An alternative situation that also might be made easier after the JOBS Act is the now common practice of a company proceeding simultaneously with a dual track of a potential sale of the company and an initial public offering until a decision is made which route to follow.

E. Pre-IPO Options

1. A product of the era of rapidly appreciating dot.com offerings was the demand of venture capitalist and other pre-IPO investors to have the right to participate in a future initial public offering. This right might take the form of a firm option similar to a preemptive right or a best efforts undertaking by the issuer to make available to the investor shares offered in a future IPO (e.g., the right to participate in a directed share program). *See* Lubowitz and Weinberg, *"IPO Participation Rights,"* INSIGHTS, July 2000 at p. 7.

2. Initially, the staff treated these pre-IPO options as a violation of § 5 and required risk factor disclosure of rescission rights. This has ceased to be the staff's position if a *Black Box* or Rule 152 analysis applies.

3. It has been the staff's position that if an IPO is commenced (i.e., filed) within one year of the grant of the pre-IPO option (whether a firm option or a best efforts undertaking), the private "offer" of the participation right before filing of the registration statement must be completed privately, either separately or as part of the IPO. If grant of the pre-IPO option is completed for purposes of Rule 152 (which may occur in this context even though the purchase price is the IPO price and the investor is therefore not at market risk) or if the investors satisfy the *Black Box* criteria of being qualified institutional buyers or two or three large institutional accredited investors, exercise of the option will not be integrated with the IPO. The securities purchased pursuant to the option would be "restricted" and eligible for resale pursuant to a resale registration statement or an exemption from registration.

4. The private bar has expressed the view that, in most cases, the prospects of an IPO are sufficiently inchoate and uncertain that an "offer" should not be considered as having made. The staff has not accepted this view yet if the IPO in fact commences within one year. It remains to be seen whether the ability to test-the-waters before the filing of a registration statement will affect this situation.

VI. PUBLIC TO PRIVATE OFFERINGS

A. Limited Public Offerings

The staff has confirmed that a registered offering to a limited number of investors is permissible and, based on the *American Council of Life Insurance* letter, the investors will not be presumptive underwriters and will receive freely tradable securities so long as they purchased in the ordinary course, were not market intermediaries and had no arrangements for redistribution. Although the *American Council of Life Insurance* letter focused on institutional investors, its principle should also apply to non-institutional investors.

B. Withdrawn Registrations

1. As stated above, the Commission's position is that the filing of a registration statement constitutes the commencement of a public offering and, in broad terms, a general solicitation. Presumably, the pendency of the registration statement may constitute a continuing general solicitation. The confidential submission of a registration statement by an emerging growth company might not present the same issue. Accordingly, the registration statement might have to be withdrawn before a private offering that would otherwise be integrated with the registered offering could be undertaken. Withdrawal of the registration statement is an express condition of the Rule 155 safe harbor. See VIII below. An alternative for a public company eligible to use Form S-3 for a primary offering might be to convert the registration statement to a generic shelf registration. See VI.D below.

2. The staff has expressed concerns over the availability of an exemption for a private offering that followed a withdrawn registration statement of the same class of securities. See the CorpFin Outline at §VIII.A.9 (first paragraph) and C&DI § 139.08; see also note 122 to the Reg. D Proposing Release.

3. In the absence of the Rule 155 safe harbor, in order to avoid integration and attribution of the registered offering's general solicitation, the private offering would have to be sufficiently separate under the five factor test. This could involve issuing a different security or waiting a suitable interval after withdrawal of the registration statement. The staff has cited the six-month integration safe harbor under Regulation D.

4. This situation could be particularly difficult for a company that files for an IPO only to have the IPO window close on it. Often, there would be a confidential submission or a "quiet filing" with no marketing activity. While not determinative, the absence of marketing activity should be a helpful factor in negating the existence of general solicitation that is attributed to the subsequent private offering.

5. Alternatives for this company may include (i) use of a different security or the passage of time in order to avoid integration and permit a private offering, as well as carefully monitoring the private purchasers, (ii) use of Regulation S for sales offshore, (iii) proceeding under the registration statement for sales to the investors to whom the securities would have been sold privately or (iv) possibly use of Rule 506(c).[1] Some companies have structured the security so that the underlying common stock cannot be acquired for at least a year in order to avoid integration with a failed registered common stock offering based on there not being a current offer of the common stock under § 2(a)(3).[2] Other companies have relied on *Black Box* and completed the private offering to *Black Box* eligible investors, either immediately if there had been no marketing activity or after waiting a suitable interval (sometimes as little as 30 days) to complete the private offering if there had been marketing activity, or they have otherwise satisfied themselves after a suitable interval that the nature of the investors was such and their relationship with the company existed independent of the marketing of the registered offering

[1] As to Regulation S offerings, see Release No. 33-7392 (Feb. 20, 1997) in which the Commission proposed amendments to Regulation S to address abusive practices and Release No. 33-7190 (June 27, 1995), an interpretive release addressing certain abusive practices. The amendments were adopted in Release No. 33-7505 (Feb. 17, 1998).

[2] A question when convertible securities are being used is whether they can be made mandatorily convertible upon an IPO which may occur within the one year period. Some believe that this should not affect the no "offer" analysis for purposes of integration since the conversion would be outside the investor's control and would not involve an investment decision. Others are concerned that the analysis of mandatorily exchangeable securities in which the sale of the underlying security is deemed to occur when the primary security is sold might be applied and result in a current offer. Given the customary nature, for the benefit of issuers, of provisions requiring mandatory conversion of convertible securities upon an IPO and the uncertainty that an IPO will occur, the staff could conclude that it is not necessary to apply the mandatorily exchangeable securities analysis in this circumstance and therefore should recognize that such a provision would not adversely affect the integration analysis.

that a private offering exemption could be relied on. See this author's article *"What Can We Do Now That Our Public Offering Has Aborted,"* INSIGHTS, July 2000 at p. 3, written before the adoption of Rule 155 or Rule 506(c).

6. The staff has sometimes shown some sympathy toward the completion of a private offering following termination of the registered offering where the investors were not contacted as part of the registered offering. The staff is likely to be unsympathetic in the case of a private offering following withdrawal of a registration statement after receipt of troublesome comments from the staff. See the *Circle Creek* letter.

7. The principles underlying the Commission's guidance in the Reg. D Proposing Release might come into play here based on a facts and circumstances analysis. If an issuer can do a private offering while a registration statement is pending, it should be able to do that same offering after the registration statement has been withdrawn, assuming the criteria for a private offering can be met.

8. Following the Comprehensive Revision Release proposal to amend Rule 152 to establish a safe harbor for doing a private offering following an abandoned registered offering, Rule 155 was adopted providing such a safe harbor. See VIII.C below.

9. The JOBS Act might provide another alternative since testing-the-waters with QIBs and institutional accredited investors is not gun-jumping in violation of § 5(c) and therefore might not foreclose switching to a private offering on a facts and circumstances analysis under the SEC's guidance or as a Rule 506(c) offering.

C. Completed Public Offering

The staff applies the same analysis to private offerings following a completed registered public offering. Accordingly, it is important to structure the subsequent private offering so that it is separate from the registered public offering under the five factor test of Release No. 33-4552 and, if necessary, the other factors relevant to negating the existence of general solicitation. The Rule 155 safe harbor does not apply to this situation. Again, the Commission guidance in the Reg. D Proposing Release could prove helpful, as might the changes under the JOBS Act.

D. Shelf Registrations

1. The staff has indicated that the pendency of a shelf registration, whether a traditional shelf of a specific security or a generic or universal shelf, would not prevent an exempt private offering from being done so long as the security being privately offered had not been taken off the shelf for offering under the registration statement. See the CorpFin Outline at § VIII.A.9 (first paragraph) and Release Nos. 33-7856, 34-42728, *"Use of Electronic Media"* (Apr. 28, 2000), at note 10.

2. The question comes up whether a resale shelf registration under which securities are actively being sold will constitute general solicitation preventing a private offering

by the issuer of similar securities. For example, if the issuer files a resale S-3 covering common stock previously privately placed with investors, may the issuer engage in a private offering of its common stock? The answer should be that a registered secondary offering ordinarily should not be integrated with a primary offering because they are for very different purposes and involve different sellers.

3. One situation where there may be a problem with the resale registration is a burst PIPE if the issuer's offering after filing the resale registration statement is deemed part of the same offering as the private placement of the securities subject to the resale registration statement, resulting in loss of the exemption. See V.B above. Another situation that can present a problem is where a broker-dealer that participated in the private placement is included as a selling shareholder under the resale S-3. The staff may take the position that the broker-dealer is acting as an underwriter and its resale is really a primary offering. The mere existence of a broker-dealer as a selling shareholder, however, should not create a problem where that broker-dealer did not participate in the private placement. The staff, however, has sometimes taken the position that any broker-dealer, and even an affiliate of a broker-dealer, is an underwriter and therefore that there is a primary offering for which the issuer may not be S-3 eligible.

VII. ACQUISITIONS AND EXCHANGE OFFERS

A. Resale Registration

The Rule 152 analysis for PIPE transactions would apply in the case of acquisitions where the private offering exemption is relied upon for the offer of the acquirer's securities as the merger consideration and a registration statement covering resales of the securities is filed before the merger is completed. A condition that could prevent the private offering from being completed is the need for shareholder approval by the acquired company. As long as there are sufficient binding voting commitments in place for the merger before the registration statement is filed, Rule 152 would be satisfied. See VII.B.

B. Voting and Tender Commitments

1. The staff has raised questions about the status of the shares as to which voting commitments to vote in favor of the merger have been obtained in negotiated acquisitions prior to the filing of the Form S-4 registration statement. It has been traditional for acquirers to seek voting commitments from key shareholders in order to increase the likelihood that the transaction will be approved and the merger consummated. The staff's concern is that a private offering took place in connection with obtaining the commitments and therefore the committed shares cannot be included under the Form S-4 for issuance in the merger but rather are restricted securities eligible for resale registration.

2. The staff has recognized traditional practice and permits shares of major shareholders, directors and key employees subject to voting commitments to be included in the Form S-4, at least in the case of public companies or companies for which the acquisition could not be done as a private offering and less than 100% of the voting shares have been locked up. See the CorpFin Outline at §VIII.A.9 (third paragraph). This position was proposed to be

codified in the Comprehensive Revision Release by the adoption of Rule 159. That rule has not been adopted, and Rule 155 does not address this situation. This position has been codified in C&DI § 239.13 (also in § 225.10). That interpretation makes clear, however, that written consents, because they are the corporate action and not executory, will be treated as a sale and thus the shares to which they relate may not be included in the subsequent Form S-4.

3. In the past, the staff sometimes was unwilling to apply this voting commitment policy to closely-held companies and even raised the question whether S-4 registration can be used at all, particularly when the committed shares are sufficient to effect the corporate action. As reflected in C&DI § 239.13, this is no longer the staff's position so long as the conditions of C&DI § 239.13 are satisfied and the commitment is a voting agreement and not a written consent that effects the corporate action.

4. An alternative for dealing with these issues is use of an acquisition shelf registration statement. *See Service Corporation International* (avail. Dec. 2, 1985).

5. In November 2009, the SEC staff extended its voting commitment position to commitments to tender in negotiated third party exchange offers and in debt exchange offers. C&DI § 139.30 extends to negotiated third party exchange offers (i.e., share for share acquisitions) the same relief as extended to voting commitments in merger or sale of assets transactions, subject to the same limitations, together with a requirement that the tender offer be made to all shareholders of the target at the same consideration. This position does not apply to unfriendly exchange offers. Thus, commitments can now be obtained from eligible shareholders in negotiated acquisitions regardless of the form of the transaction. C&DI § 139.29 extends this relief to debt exchange offers so long as commitments to exchange are limited to accredited investors who own less than 100% of the particular series and the tender offer will be made to all holders of that series at the same consideration. This position eliminates the impediment that existed for registered debt exchange offers that was caused by the inability to obtain market-tested commitments from key debtholders. In both cases, actual tenders and signing letters of transmittal are not permitted. See this author's article "*SEC Expands Position on Use of Lock-Up Agreements*," INSIGHTS, January 2010 at p. 35.

VIII. THE INTEGRATION SAFE HARBORS UNDER RULE 155

A. General Provisions

1. Rule 155 adopted in the 2001 Release establishes two safe harbors, one for doing a registered public offering after terminating a private offering (Rule 155(b)) and the other for doing a private offering after terminating a registered public offering (Rule 155(c)). It is important to recognize that these are non-exclusive safe harbors and therefore their adoption adds to, rather diminishes, the alternatives that otherwise exist for avoiding integration in these situations. *See* Harms, *Integration Under The 1933 Act: The SEC Provides New Safe Harbors*, 34 Review of Securities & Commodities Regulation 259 (2001). Thus, the Commission's guidance in the Reg. D Proposing Release might provide alternatives in some circumstances to the Rule 155 safe harbors. Similarly, the changes under the JOBS Act might offer increased flexibility. See IX below.

2. Rule 155(a) limits the rule's relief to private offerings under § 4(a)(2), including pursuant to Rule 506 of Regulation D, and § 4(a)(5) of the Securities Act. A Rule 144A offering would qualify as a private offering. The rule does not apply to §3(b) limited offerings under Rules 504 or 505 of Regulation D because investors in those offerings may be neither accredited nor financially sophisticated. The rule also does not apply to the State Accredited Investor Exemption. The reason given in the 2001 Release is that this exemption permits general solicitation and is therefore not a private offering (the JOBS Act provides that general solicitation in a Rule 506 offering does not result in its being a public offering).

3. A preliminary note to the rule provides that the safe harbors are not available if they are used as part of a plan or scheme to evade registration. For example, Rule 155(b) may not be used for purposes of testing the waters to determine investor interest for a public offering. Rather, there must be a bona fide intention to conduct a private offering. Correspondingly, using a registered offering to generate publicity for the private offering would be such a plan or scheme. It remains to be seen how the ability for an emerging growth company to test-the-waters will affect this.

4. Rule 155 does not deal with the general integration concept, the five factor test or the *Black Box* analysis. Nor does it deal with completed private offerings and PIPE transactions involving filing of a resale registration statement or with completed public offerings. These areas remain unaffected. In addition, Rule 155 does not deal with voting commitments in merger transactions, which Rule 159 proposed in the Comprehensive Revision Release sought to address.

B. Private to Public Safe Harbor

1. Rule 155(b) provides a safe harbor for an abandoned private offering followed by a registered offering if four conditions are met. The conditions are designed to insure that there is a separation in the two offerings and that investors understand this separation.

2. The first condition is that no securities may be sold in the private offering. This sounds simple but it may not be. What if the private offering is being sold in tranches? If part of the same offering, the sale of some securities would make the safe harbor unavailable. However, even though the safe harbor of Rule 155(b) might be unavailable, Rule 152 could be available if the private offering is completed through a combination of the sale of securities in the first tranches and the termination of the remainder of the offering. Similarly, a traditional integration analysis might result in an earlier offering being treated as part of the current offering, causing a loss of the safe harbor. But again, Rule 152 might apply. Another issue involves how far you can go with the private offering before it is deemed "completed," making the safe harbor unavailable. For example, what if an investor orally commits to purchase in the private offering and another investor subsequently indicates it is prepared to invest only if the offering is registered Assuming that there was a bona fide intention to conduct a private offering and the first investor is not contractually bound, the company should be able to abandon the private offering and complete the transaction with these investors as a registered offering

using the safe harbor. The 2001 Release indicates that providing this flexibility is one of the purposes of the safe harbor.

3. The second condition is that all offering activity in the private offering cease before the registration statement is filed. If the company is using agents to identify investors, it must make sure the activities of these agents cease. A question is whether a company can use the safe harbor to do a takedown from an existing shelf registration after terminating the private offering activity? The staff has indicated that the rule does not apply to shelf registrations. Nevertheless, Rule 152 might be available since a company is not treated as being "in registration" because of a generic shelf registration when there has not been a takedown.

4. The third condition is that the preliminary and final prospectus disclose the size and nature of the private offering, the date it was abandoned, that any offers to buy or indications of interest in the private offering were not accepted and that the prospectus supersedes any offering material used in the private offering. These disclosures need be made only to investors in the public offering entitled to receive a prospectus. They do not need to be furnished to the private offerees.

5. Finally, the registration statement may not be filed for 30 days after termination of all private offering activity unless all offerees were or were reasonably believed by the company to be accredited investors or financially sophisticated within the meaning of Rule 506. Although this would require keeping track of the status of offerees, the requirement applies only if the company wants to be able to file before waiting 30 days. In many controlled private offerings, it may not be difficult to identify who were offerees and their status as accredited or sophisticated.

6. The SEC indicated that it will monitor the use of the Rule 155(b) safe harbor, and will likely be asking in comment letters on the registration statement for information about termination of private offering activity and, if the filing is within 30 days, about the private offerees.

C. Public to Private Safe Harbor

1. Rule 155(c) establishes a safe harbor for conducting a private offering after an abandoned registered offering. This safe harbor gives companies an important new alternative for doing an exempt private offering following an aborted public offering.

2. There are five conditions to be met for the safe harbor. These conditions are designed to assure that the private offering is separate and distinct from the registered offering and that offerees in the private offering are aware of the more limited legal protections they receive in the private offering. The first condition is that no securities be sold in the registered offering. The receipt of funds or placing funds in escrow will prevent this condition from being met.

3. Second, the registration statement must be withdrawn. As discussed below, withdrawal has been made easier. A question is whether this condition can be met in the case of

a shelf registration without withdrawal, for example by terminating the public offering and putting the securities back on the shelf? The staff has indicated that the safe harbor would not be available in this situation. However, it might be possible to terminate the public offering from the shelf and conclude under a traditional integration analysis, including the five-factor test and the *Black Box* policy position, that an exempt private offering can be undertaken without reliance on the safe harbor. The principles underlying the Commission's guidance in the Reg. D Proposing Release, as well as the JOBS Act changes, might be helpful in this analysis.

4. Next, the private offering may not be commenced until 30 days after the withdrawal of the registration statement.[3] This condition applies for purposes of the safe harbor regardless of the nature of the investors. However, if a company wants to undertake the private offering without waiting the 30 days or satisfying the other conditions of the safe harbor, it may be able to do so using the existing alternatives, such as the *Black Box* analysis and perhaps the Reg. D Proposing Release guidance. The basic principle of that guidance permitting a facts and circumstances analysis of whether the investors were obtained through the general solicitation attributable to the registered offering should apply to this situation. See II.D.6 above. In addition, a company may be able to use Rule 506(c) for sales solely to accredited investors whose status it verifies.

5. Fourth, each offeree in the private offering must be notified that the offering is not registered, that the securities are restricted, that purchasers do not have the protection of § 11 of the Securities Act and that a registration statement was filed and withdrawn, specifying the withdrawal date. Unfortunately, the Commission reintroduced the concept of "offeree" that had been eliminated under Regulation D. Consequently, a determination of what constitutes an offer and the tracking of offering activity will be required. This condition adds unnecessary uncertainty to the availability of the safe harbor, and it would be helpful if the SEC interpreted it as applying to each purchaser and to each other investor furnished a private placement memorandum.

6. The final condition is that any private placement memorandum that is used disclose any material changes in the company's business or financial condition since the registration statement was filed. This condition does not, by its terms, seem to require a disclosure document, although one might be used to comply with antifraud rules.

7. The SEC staff has stated that the rule provides a safe harbor only from integration and that the private offering must meet the requirements for a valid exemption, including (to the extent it is applicable) the absence of general solicitation. In a key paragraph of the 2001 Release, the Commission stated:

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[3] This 30-day period, along with the 30-day safe harbor periods proposed in the Comprehensive Revision Release for offerings following abandoned private and public offerings, has influenced the time periods with which practitioners feel comfortable for purposes of treating offerings as separate.

> We believe that ordinarily an issuer would not be inclined to incur the costs of preparing and filing a registration statement with the intention to withdraw it later and commence a private offering. Nevertheless, we wish to assure that issuers do not use this integration safe harbor merely as a mechanism to avoid the private offering prohibition on general solicitation and advertising. At the time the private offering is made, in order to establish the availability of a private offering exemption, the issuer or any person acting on its behalf must be able to demonstrate that the private offering does not involve a general solicitation or advertising. Use of the registered offering to generate publicity for the purpose of soliciting purchasers for the private offering would be considered a plan or scheme to evade the registration requirements of the Securities Act.

This proscription may not apply to offering activity that both fits within the ability to test-the-waters and engage in a general solicitation under the JOBS Act changes, but it will continue to apply otherwise. Absent a plan or scheme to evade registration, the question is the extent to which marketing activity in the public offering will affect the availability of the exemption for the subsequent private offering? It is clear that neither the general solicitation arising from the filing of the registration statement nor the fact that marketing activities, such as a roadshow, generally took place would defeat the exemption. Rather, the staff has indicated that a facts and circumstances analysis would apply. Relevant factors should include the nature of the investors, when the marketing activity occurred, whether the issuer or an underwriter had a pre-existing relationship with the investor at the time of the marketing in the public offering or whether such a relationship existed at the time of the private offering. For example, if the securities were marketed in the public offering to the customers of the underwriter or to well-known institutional investors, the sale of the securities to these investors in the subsequent private offering should not raise general solicitation concerns. On the other hand, if a list was compiled of potential retail investors with which neither the underwriter nor the company had a relationship and no relationship was then established, the inclusion of those investors in the private offering might raise concerns about general solicitation. It is important that practitioners and the staff apply these factors in a way that fosters the Rule 155(c) safe harbor's purpose of enabling issuers to complete a private offering and reduce the financial risk of an abandoned public offering by permitting the two offerings to be separated. This is consistent with the purpose of the Commission's guidance in the Reg. D Proposing Release, as well as the JOBS Act changes.

D. Withdrawal of Registration Statement

1. The Commission amended Rule 477 to permit an issuer to withdraw a registration statement before it becomes effective without SEC approval. The withdrawal is effective automatically upon filing unless the SEC objects within 15 days. This change will facilitate the ability of issuers to rely on Rule 155(c) without encountering administrative delays. If the registration became effective, SEC approval will be necessary, but the SEC has indicated that it will expedite its approval of the withdrawal. Withdrawal of the registration statement also withdraws any Form 8-A filed under the Exchange Act.

2. Rule 477 requires the issuer to state that no securities were sold in the offering and, if the issuer anticipates relying on Rule 155(c), that it may do so. However, the issuer may not discuss the terms of the anticipated private offering because that might result in a general solicitation. Importantly, stating an intention to rely on Rule 155(c) in the withdrawal application is not a condition to use of the safe harbor.

3. There is no refund of the filing fee on withdrawal. However, Rule 457 was amended to permit the issuer to apply the fee to any registration it, its majority-owned subsidiaries or its parent may file within five years. Rule 457 was also amended to codify certain staff interpretations regarding fees. Rule 429 was amended to move its fee provisions to Rule 457, leaving Rule 429 to deal solely with use of a combined prospectus for more than one registration statement.

IX. IMPACT OF THE JOBS ACT

A. JOBS Act Changes

1. The two key principles underlying the SEC's position that an offering must be both commenced and completed either privately or publicly are general solicitation from a public offering that would prevent completing it privately and gun-jumping that would prevent converting a private offering into a public offering. The JOBS Act creates exceptions to these two principles by directing the SEC to amend Rule 506 to permit general solicitation if sales are made solely to verified accredited investors, which the SEC has done (see II.E.2 above), and authorizes (without SEC rulemaking) test-the-waters activity by a new category of "emerging growth companies" with QIBs and institutional accredited investors before or after the filing of a registration statement. These changes affect the integration analysis when they apply. For example, if there is widespread general advertising in connection with a completed Rule 506(c) offering sold only to accredited investors, will Rule 152 apply to permit a subsequent registered public offering or will the general advertising be considered gun-jumping? In my view, the answer should be that Rule 152 does apply and compliant general advertising should not be treated as impermissible gun-jumping.

2. In addition, these permitted activities can create integration issues for related offerings under traditional integration concepts and reduce the flexibility companies otherwise would have. For example, general solicitation activity in a Rule 506(c) offering could prevent completing the offering to non-accredited investors and may foreclose use of other exemptions outside Rule 506(c), such as the statutory 4(a)(2) private offering exemption or Rule 506(b), in which general solicitation is not permitted. Similarly, test-the-waters activity could constitute general solicitation that would foreclose some exempt offerings.

3. In addition to raising issues under § 5 of the Securities Act, integration concepts can raise issues under the antifraud provisions. For example, in the situation described in paragraph 1 above, even if the general advertising is not gun-jumping, will it be considered a written offer in connection with the registered offering for which there can be antifraud liability? Similarly, can test-the-waters communication be the basis for antifraud liability in a subsequent

registered offering in which the institutional investors purchase or in a Rule 506(c) offering to them?

4. In its amendment of Rule 506 and Rule 144A, the SEC has chosen to limit the amendments to those required to implement the JOBS Act and not to get into broader issues involving private and other exempt offerings, including generally integration issues arising from the JOBS Act changes. Rather, the Commission has indicated that these issues will be considered separately. The Commission did provide transition guidance in the Rule 506 Adopting Release at p. 19. *See also* C&DI §§ 260.05, 260.11, 260.12, 260.33 and 260.34. The Commission also has addressed integration issues in the release proposing the revision of Regulation A mandated by the JOBS Act. See Release No. 33-9497, *"Proposed Rule Amendments for Small and Additional Issues Exemptions Under Section 3(b) of the Securities Act"* (Dec. 18, 2013), at pp. 55-60; see also Release No. 33-9470, *"Crowdfunding"* (October 23, 2013), text accompanying fn. 33-34. The Commission states in the Regulation A proposing release at p. 57 that "… we believe that an offering made in reliance on Regulation A should not be integrated with another exempt offering made by the issuer, provided that each offering complies with the requirements of the exemption that is being relied upon for the particular offering." It then gives examples of a concurrent offering for which general solicitation is not permitted (citing the Reg. D Proposing Release interpretation) and one for which it is. This approach may be a harbinger of further SEC clarification on integration following the JOBS Act changes. *See also* Release No. 33-9741, *"Amendments for Small and Additional Issues Exemptions under the Securities Act"* (March 25, 2015), § II.B.5.

B. Application to Specific Situations

1. Consider the case of a company that recently (and after the effective date of the Rule 506 changes) completed an exempt offering under § 4(a)(2), Rule 505 or Rule 506(b) and now wants to do a Rule 506(c) offering solely to accredited investors using general solicitation. If applying the five-factor test the offerings would be integrated under traditional integration principles the general solicitation in the subsequent offering might relate back and defeat the exemption for the prior offering, and the presence of non-accredited investors might defeat the Rule 506(c) offering exemption. In view of Congress' intent to facilitate capital formation, it would be helpful for the SEC to take action, whether through rulemaking or guidance, to separate these offerings by confirming that a completed exempt offering is not affected by a subsequent Rule 506(c) offering solely to accredited investors (akin to Rule 152 or Rule 251(c)) or by reducing the integration safe harbors from 6 months to 90 days as previously proposed or even less. Although § 4(b) of the Securities Act provides that a Rule 506 offering is not a public offering as a result of general solicitation, that offering has attributes of a public offering, namely the general solicitation, that are relevant to the purpose of Rule 152 and therefore one possibility might be to apply Rule 152 to this situation. The SEC did indicate in the Rule 506 Adopting Release at p. 19 that general solicitation under Rule 506(c) after the effective date will not affect the exempt status of offers and sales made prior to the effective date in reliance on Rule 506 as it then existed (and now is Rule 506(b)). Chairman White also indicated in a letter dated August 8, 2013 to Congressman McHenry, *avail. http://www.wowlw.com/White%20Response%20to%20McHenry%20Letter.pdf*, that any

proposed revision of Rule 506 would not apply to offerings prior to the effective date of such revision and so issuers could comfortably rely on Rule 506(c) as currently adopted. On January 23, 2014, the staff issued C&DI §§ 260.33 and 260.34 providing further transitional guidance. If an issuer begins a Rule 506 offering before the September 23, 2013 effective date and after that date continues the offering under Rule 506(c), it must only take reasonable verification steps for investors who purchase after the effective date in the Rule 506(c) offering and not those who purchased before. If the issuer sold to non-accredited investors before or after September 23, 2013 in reliance on Rule 506 or Rule 506(b), it may continue the offering in reliance on Rule 506(c) without impairing the exemption for the prior sales so long as subsequent sales are limited to accredited investors for which the issuer has taken reasonable verification steps. In my view, this same approach should apply to an offering commenced pursuant to Rule 506(b) (as well as other exemptions that do not permit general solicitation) after September 23, 2013. It would be helpful if the SEC confirmed this.

2. Alternatively, a company might begin an exempt offering without general solicitation but before any sales are made decide to convert to a Rule 506(c) offering. This should be permissible. See C&DI § 260.12. See also by analogy Rule 155(b), although it is not obvious that all its conditions are necessary.

3. Consider the reverse situation, with a company that completes a Rule 506(c) offering using general solicitation and within 6 months wants to do an exempt offering under § 4(a)(2), Rule 505 or Rule 506(b) with sales to non-accredited investors. Again, traditional integration principles could prevent the subsequent offering from being exempt because of the general solicitation. Here, too, it would be helpful for the SEC to provide relief, for example, by making clear that a facts and circumstances analysis can be used under the guidance in the Reg. D Proposing Release. In addition, a safe harbor like Rule 251(c) might be considered.

4. Alternatively, what if, rather than completing the Rule 506(c) offering, the company abandons it after engaging in general solicitation but now wants to raise funds from non-accredited investors apart from the general solicitation. Again, it would be helpful if the SEC clarified that a facts and circumstances analysis can be applied to demonstrate that the non-accredited investors were not found through the general solicitation. In addition, the Commission could consider a safe harbor along the lines of Rule 155(c).

5. Another situation is a company that undertakes a Rule 506(c) offering using general solicitation and decides to convert to a registered offering or to do a side-by-side or follow-on registered offering. It would be helpful for the SEC to provide guidance for these situations. For example, if a Rule 506(c) offering is completed, Rule 152 should be applicable to permit a follow-on registered offering for the reasons identified above. Similarly, if the Rule 506(c) offering is abandoned, a registered offering should be possible if the company can conclude that there was no impermissible gunjumping. Rule 163A, for example, might be available in such a situation to avoid gunjumping.

6. The changes to Regulation D adopted by the Commission require checking a box on Form D to indicate whether the offering is under Rule 506(b) or Rule 506(c). Aside from

the question of what are the consequences of checking the wrong box, the question is raised whether checking the 506(c) box is itself general solicitation. The answer should be that checking the box in a filed Form D should not itself be general solicitation absent other solicitation activity. See C&DI § 260.11.

7. A company does a crowdfunding offering under § 4(a)(6) (once rules, which have been proposed, are adopted creating the exemption) and complies with the limitations on the offering process required by § 301 of the JOBS Act. It may have done a Rule 506(c) offering with general solicitation before commencing the crowdfunding offering, it may want to do a side-by-side Rule 506 offering or it may want to raise additional capital with a follow-on Rule 506 offering, with or without general solicitation. Alternatively, the company could be doing a Regulation A offering as revised in accordance with § 401 of the JOBS Act. These situations should be addressed in connection with the crowdfunding and Regulation A rulemaking, as proposed by the Commission, including confirmation that a prior or contemporaneous Rule 506 (or other exempt) offering does not affect the crowdfunding amount limitation under § 4(a)(6)(A). See A.4 above.

8. An emerging growth company, following filing of a registration statement, has test-the-waters communications with several institutional accredited investors to determine their interest in investing in the company and finds that these investors want to invest before the public offering occurs. Since these communications are not gun-jumping, the company should be able to complete a Rule 506 offering solely with these investors, either as a Rule 506(b) offering or a Rule 506(c) offering depending on the circumstances. This should be the case even if marketing activity has occurred, especially if Rule 506(c) is used. Even before amendment of Rule 506, it was possible to complete the private offering applying a facts and circumstances analysis as permitted by the Reg. D Proposing Release. It would be helpful if the SEC made clear that testing-the-waters by an emerging growth company under § 5(d) of the Securities Act, whether before or during the pendency of a registration statement, will not prevent a company from engaging in an exempt offering so long as the requirements for testing-the-waters are met and the requirements for the exempt offering are otherwise met. Furthermore, because the permissible test-the-waters communication is not gun-jumping, an institutional accredited investor's participation in an exempt private offering should not prevent it from buying in the public offering.

9. As a result of the amendment of Rule 144A, a company can conduct a Rule 144A offering using general solicitation following a private offering under § 4(a)(2) to the initial purchasers. As recognized in the Rule 506 Proposing and Adopting Releases, the general solicitation in the 144A offering would not affect the exemption for the offering to the initial purchasers because of Rule 144A(e). Furthermore, so long as the initial offering was done under Rule 506(c) and the initial purchasers were accredited investors, as they typically would be, there should no longer be any hesitation to provide a copy of a prospectus used in a contemporaneous registered public offering to investors in a 144A offering.

10. A company that does a side-by-side Regulation S offering abroad can do a Rule 506(c) or 144A offering in the United States using general solicitation. The Commission

has addressed the issue of the potential integration of these offerings in Section IV of both the Rule 506 Proposing and Adopting Releases. The Commission has confirmed that the existing position reflected in Rule 500(g) and the note to Rule 502(a) that offshore sales under Regulation S will generally not be integrated with a domestic offering will continue to apply notwithstanding the use of general solicitation for the domestic offering and that the general solicitation should not be considered impermissible U.S. directed selling efforts under Regulation S so long as the offerings are conducted in compliance with their applicable exemptions.

11. The Commission's proposals to further revise Regulation D would create even greater challenges in dealing with integration issues. For example, the proposals to require advance filings and additional information if general solicitation is used can make it harder to know what exemption is available if general solicitation is unplanned. Moreover, the disqualification provision if the Form D filing requirement is not satisfied means that every prior offering during the lookback period would need to be examined to determine if Rule 506 is available to exempt the current offering.

X. CONCLUSION

The Commission's adoption of Rule 155 and its guidance in the Reg. D Proposing Release, as well as several recent C&DIs, were helpful steps forward in bringing added clarity and certainty to some of the issues involved in the integration of private and public offerings. The JOBS Act and SEC rulemaking under it has added a new set of issues that deserve attention. The Commission should continue to analyze the basic principles underlying the treatment of public/private offerings, as well as the appropriate approach to integration generally, and should provide guidance as to how the JOBS Act affects the various issues in this area, in each case with a view to implementing the intent of Congress reflected in the JOBS Act to facilitate capital formation while preserving the necessary level of investor protection.

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