

The following is a summary of SEC Release No. 33-8501: the Securities and Exchange Commission's Securities Offering Reform Proposal.

The way issuers raise capital has changed over the course of the past several years, and the SEC has announced proposals for modernizing and liberalizing the securities rules so that issuers raising capital may do so in an efficient manner through registered offerings, while maintaining a high level of investor protection through an issuer's dissemination of complete and timely information regarding its business and its securities. As such, the proposed modifications to the securities laws are predicated upon the relatively new information capabilities - in terms of the speed of dissemination to a widespread audience - that are available today, that were not available when the current rules were enacted. The new proposed rules complement the SEC's increased focus on their review of reports filed pursuant to the Securities Exchange Act of 1934 (the "Exchange Act"). The proposals generally modify three main areas of the securities rules: communications related to registered securities offerings; procedural restrictions in the offering and capital formation processes; and delivery of information to investors.

Categories of Issuers

The proposed rules offer differing amounts of flexibility to different categories of issuers with respect to communications and registration procedures.

Well-known seasoned issuers ("WKSIs") by their nature, and in the current environment, tend to have more extensive and more reliable information available about them than do other issuers, and therefore, they will be given the greatest flexibility with respect to communications and offerings. WKSIs are issuers that:

- are required to file Exchange Act reports;
- are current in their SEC reporting obligations (and have been timely in their reports for the preceding twelve months);
- are eligible to use Form S-3 or F-3; and
- have either (i) a market capitalization at prior year end of \$700 million, in which case it will be a WKSI in all cases or (ii) issued \$1 billion of debt securities in registered offerings during the past three years, in which case it will be a WKSI only with respect to non-convertible debt securities.

Issuers in the other general categories: **seasoned issuers** (those eligible to use Form S-3 or F-3, but who do not meet the other WKSI requirements); **unseasoned Exchange Act reporting issuers** (those required to file Exchange Act reports, but that do not qualify to file on Form S-3 or F-3); and **non-reporting issuers** (those not required to file Exchange Act reports - i.e. those involved in an IPO), will generally be afforded respectively less flexibility with respect to communications and offerings. **Voluntary Exchange Act report filers** will be treated as unseasoned reporting issuers for purposes of the new rules. Under the new rules, issuers that file Exchange Act reports voluntarily will need to disclose that fact on the front cover of their filings to alert the public that the issuer might discontinue their reporting and that they are not eligible to use automatic shelf procedures.

Communications Related to Registered Securities Offerings

Currently, the securities laws provide tight restrictions on written and oral communications during various stages of registered public offerings ("gun-jumping" provisions). Under the proposed rules:

- all forms of communications, other than direct oral communications (regardless of the medium, including a telephone or the internet) will be defined as written communications for purposes of the Securities Act of 1933 (the "Securities Act"). The intention is to capture under the heading "writing" future communication technology that is not of an oral nature.
- **WKSIs** will be permitted to use oral and written communications at any time before, after or during a securities offering, subject to certain filing requirements;
- Two safe harbors will be created:
 - **seasoned issuers and unseasoned Exchange Act reporting issuers** will be permitted to publish regularly released factual business information and forward-looking statements;
 - **non-reporting issuers** will be permitted to publish regularly released factual business information (but not forward looking statements) to everyone other than investors (e.g. to customers and suppliers);
- communications made more than 30 days before the filing of a registration statement by or on behalf of an issuer will be permitted, so long as they do not reference the offering;
 - Trap for the unwary: issuers will need to take reasonable precautions to prevent further dissemination of the communication during the 30-day period prior to filing - if precautions are not taken, a cooling-off period might be required;
- the basic information about the issuer and its securities as well as procedural information about an offering allowed to be given under a Rule 134 notice will be expanded to include a broader range of information, but will still not permit a detailed term sheet or a hyperlink to any other prohibited information (although the detailed term sheet will be permitted if the requirements for a free writing prospectus were met);
- broader categories of routine communications will be excluded from the definition of "prospectus" (e.g. the schedule for an offering or account opening procedures); and
- exemptions for research reports will be expanded to allow offering and non-offering brokers and dealers, under certain circumstances, to publish research during an offering without violating the securities laws.

Free Writing Prospectuses

A free writing prospectus is defined as any written communication that constitutes an offer to sell securities that are or will be the subject of a registration statement that is not a prospectus satisfying the requirements of Securities Act. The new rules generally permit a responsible level of communication with investors regulated by the accuracy of the content, as opposed to being prohibited without regard to the accuracy of the content. After a registration statement is filed, all offering participants, including issuers and underwriters, will be permitted to use free writing prospectuses. Depending on the nature and the provider of a free writing prospectus, it generally will need to be filed with the SEC at or prior to the time, it is distributed.

- **Seasoned issuers**, and in some cases **WKSIs**, will be required to include a legend on their free writing prospectuses referencing, among other things, the statutory prospectus. In cases where legends may not be available (for example, in certain media), the copy filed with the SEC needs to include the legend. Therefore, advertisements and broadcasts will be feasible for these types of issuers.
- Non-WKSI **seasoned issuers** will be permitted to use free writing prospectuses so long as they have a statutory prospectus on file with the SEC.
- **Non-reporting issuers and unseasoned reporting issuers** will be required to deliver a statutory prospectus prior to or with a free writing prospectus (a hyperlink will be sufficient). Therefore, commercials, advertisements and broadcasts will generally not be feasible for offerings by issuers of this

type, but advertisements in an email with a link to a statutory prospectus will be permitted.

- Materials prepared and published by the media and not paid for by the issuer, will be treated as a free writing prospectus, but will not need to be preceded or accompanied by a statutory prospectus.

Electronic Road Shows

Although electronic road shows will fall under the definition of free writing prospectuses, in order to encourage their use, the SEC is not requiring an issuer to file the script of the road show if it does not include any material issuer information not previously filed and if the issuer concurrently makes a version of a bona fide road show available electronically to any potential investor and files any other issuer free writing prospectus or material issuer information used at an electronic road show. The bona fide electronic road show should cover the same general subjects as an issuer's other electronic road shows. Live road shows will continue to be considered oral communications.

Regulation FD

Regulation FD will also be amended, and generally will not apply to disclosures made in a free writing prospectus used after the filing of a registration statement.

Liability Issues

Under the proposed rules, for purposes of liability under Section 12(a)(2) and Section 17(a)(2) of the Securities Act, the determination of whether a material misstatement or omission exists will be made based upon the information provided to an investor at the time of its investment decision (i.e. at the time of the contract for sale). For purposes of Section 12(a)(2), a person's knowing of such untruth or omission means its knowledge as of the time of the sale as well. For shelf offerings, the effective date for disclosure liability purposes will occur at each shelf takedown, at the earlier of the date of the first use of a prospectus supplement or the time of sale.

It is anticipated that appropriate liability associated with the expanded communications will be maintained as well. For example, free writing prospectuses will have the same liability as that

which currently applies to oral offers and statutory prospectuses; written communications not constituting prospectuses will not be subject to disclosure liability applicable to prospectuses, but will still be subject to the anti-fraud provisions of the federal securities laws.

Revisions to Registration and other Procedures in the Offering and Capital Formation Processes

Revisions to the Shelf registration process:

The proposed rules modify shelf registration generally to make the process more efficient. The proposed rules:

- codify the information that is to be included in and omitted from base prospectuses and final prospectuses in shelf registration statements, including an amendment to Forms S-3 and F-3 that allows all issuer and securities information to be incorporated by reference from Exchange Act reports and including a rule that will allow seasoned issuers to identify selling stockholders in the resale of restricted securities after the effectiveness of a registration statement in a prospectus supplement;
- clarify that prospectus supplements will now be deemed to be part of and included in the registration statement containing the base prospectus and that issuers are permitted to use prospectus supplements rather than post-effective amendments to make material changes to the plan of distribution;
- eliminate certain current shelf registration requirements, including the elimination of the two year limitation for a delayed offering, the elimination of at-the-market offering restrictions (such as volume limits and identifying underwriters in the registration statement) and the elimination of the prohibition against immediate takedowns off of shelf registration statements.

Automatic shelf registration for WKSIs:

Under the automatic shelf registration process, eligible WKSIs can register unspecified amounts of different classes of securities (defined very broadly, e.g., debt, equity, warrants, units and preferred

stock) on an automatically effective Form S-3 or F-3, and such issuers will be able to add additional classes of securities and eligible majority-owned subsidiaries as additional registrants after an automatic shelf registration statement has already become effective. All automatic shelf registration statements and their post-effective amendments will become effective automatically upon filing, without SEC review. A new automatic shelf registration statement will need to be filed every three years.

Under the new rules, automatic shelf registration will also have the following advantages:

- eligible WKSIs could freely accommodate both primary and secondary offerings using an automatic shelf registration;
- filing fees could be paid in advance or at the time of a shelf takedown (on a "pay-as-you-go" basis);
- an automatic shelf registration base prospectus can omit more information than is permitted for a regular shelf registration base prospectus, and the omitted information will then be included in the relevant prospectus supplement.
- Exceptions include the addition of a new class of securities or new eligible issuers (including guarantors), which will need to be done by post-effective amendment. Other disclosure can be provided in a post-effective amendment, in a prospectus supplement deemed part of and included in, or in an Exchange Act report incorporated by reference into, the registration statement.

In summary, the differences between the base prospectus of regular shelf filers and automatic shelf filers will be that regular filers' base prospectuses will have a plan of distribution (that could be changed by prospectus supplement instead of post-effective amendment) a description of securities and a list of known selling stockholders, if applicable, and base prospectuses of automatic filers will have no plan of distribution, very minimal description of securities and no allocation of primary or secondary securities (or selling stockholders).

Additional changes to the registration process for unseasoned issuers and non-reporting issuers:

Proposed changes include expanding situations where issuers may incorporate by reference from their Exchange Act reports (for example, eligible issuers may incorporate by reference from their Exchange Act reports onto Forms S-1 and F-1 if their Exchange Act reports and other documents are current and made readily accessible on their websites) and eliminating the then-superfluous Forms S-2 and F-2.

Delivery of Information to Investors: Access to electronic documents.

- **Access equals delivery:** a prospectus is deemed to precede or accompany a security for sale as long as a final prospectus has been filed with the SEC as part of the registration statement (via EDGAR). Issuers will no longer need to deliver paper copies of prospectuses to investors in order to satisfy their Securities Act prospectus delivery obligations. In lieu of a prospectus, a notice must be sent to each purchaser, and the purchaser must be given the opportunity to request a final prospectus. Also, dealers can rely on the access equals delivery rule with respect to after market delivery obligations, other than for blank check companies. Furthermore, confirmations and notices of allocations could be sent (by email) after the effectiveness of a registration statement without being accompanied or preceded by a final prospectus.
- In the free writing prospectus context, with respect to the obligation to deliver a statutory prospectus, access will equal delivery for seasoned issuers, but non-seasoned issuers will still be required to deliver (or provide a hyperlink for) a statutory prospectus with or before the delivery of a free writing prospectus.

Additional Exchange Act disclosure proposals

Additional Exchange Act disclosure proposals include the following:

- extending risk factor disclosure to Exchange Act filings, including annual reports and updates, if necessary, in quarterly filings; and

- requiring all accelerated filers to disclose in their annual reports SEC comments made in connection with their review of an issuer's Exchange Act reports that the issuer believes are material that were issued more than 180 days before the end of the fiscal year covered by the annual report, and which remain unresolved as of the date of the annual report.

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Issuers who are, or were, in bankruptcy, blank check companies, penny stock issuers or shell companies, among certain other issuers, will not be eligible to take advantage of the flexibility provided in the communications, offering, and delivery proposals described above. Additionally, the new rules generally do not apply to business combination transactions. The SEC release also separately describes how the proposals outlined above will apply specifically to issuers of asset-backed securities.

Should you have any questions about the matters addressed in this issue of the Corporate Governance Alert, please contact the following Kirkland & Ellis authors or the Kirkland & Ellis partner you normally contact.

Vincent Pisano
vpisano@kirkland.com
(212) 446-4980

Michael Okon
mokon@kirkland.com
(212) 446-4996

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