The SEC's Securities Offering Reforms

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The SEC has overhauled the securities offering process with the broad goal of improving capital formation and modernizing offering communications, while preserving investor protection and avoiding unnecessary impediments to the capital formation process. See Release No. 33-8591 (SEC 2005), FED. SEC. L. REP. ¶87,421. The new rules are focused primarily on constructive, incremental changes in the regulatory structure and the offering process rather than the introduction of a far-reaching new system. The reforms involve three main areas: communications related to offerings; registration; and the delivery of information to investors. They take effect December 1, 2005.

The new regime is designed to:

- facilitate greater availability of information to investors and the market with regard to all issuers;
- eliminate barriers to open communications that have been made increasingly outmoded by technological advances;
- reflect the increased importance of electronic dissemination of information, including the use of the Internet;
- make the capital formation process more efficient; and
- define more clearly both the information and the timeliness of the availability of information against which a seller's statements are evaluated for liability purposes.

For purposes of the rules, the SEC categorized issuers into several tiers, consisting of non-reporting issuers, unseasoned issuers, seasoned issuers, and well-known seasoned issuers. The first three tiers of issuers are identified by pre-existing criteria under the existing federal securities laws. A "non-reporting issuer" is an issuer that is not required to file Exchange Act reports. An "unseasoned issuer" is an issuer that is required to file Exchange Act reports, but does not satisfy the requirements of Form S-3 or Form F- 3 for a primary offering of its securities.

A "seasoned issuer" is an issuer that uses Form S-3 or Form F-3 to register primary offerings of securities. The characteristics of the last tier of issuer, called well-known seasoned issuers in the rules, will be easily measurable and readily available so that issuers and market participants can determine eligibility easily.

Well-Known Seasoned Issuers

The companies that will benefit the most from the new regime are what the SEC calls well-known seasoned issuers. These are large companies followed by sophisticated institutional and retail investors, members of the financial press, and numerous analysts

actively seeking new information about them on a continual basis. Unlike smaller or less mature issuers, large seasoned public issuers tend to have a more regular dialogue with investors and market participants through the media. Further, their communications are subject to scrutiny by investors, the press and analysts.

The new rules provide well-known seasoned issuers with greater flexibility in registering their securities offerings under a more streamlined registration process known as automatic shelf registration. Under the automatic shelf registration process, eligible well-known seasoned issuers can register, on a more flexible basis than is currently the case, offerings of different types of securities using Form S-3 or Form F-3 registration statements that are effective upon filing.

In addition to filing Exchange Act reports, a well-known seasoned issuer must have a market value of $700 million or more or must have issued for cash more than an aggregate of $1 billion in non-convertible securities, other than common equity, through registered primary offerings over the prior three years. Further, the issuer must not be an ineligible issuer as defined by Rule 405. Also, investment companies and business development companies are excluded from being well-known seasoned issuers.

Whether a company satisfies the eligibility requirements for being a well-known seasoned issuer generally will be determined on an approximately annual basis.

A company that meets the definition of well-known seasoned issuer based on the $700 million public float threshold can use an automatic shelf registration statement to register any offering of securities, other than those for business combination transactions. A company issuer that meets the definition of well-known seasoned issuer based on the amount of registered non-convertible security issuances in the prior three years also may register any such offering for cash using automatic shelf registration if it is eligible to register a primary offering of its securities on Form S-3.

Under the SEC rules, ineligible issuers are:

- reporting issuers who are not current in their Exchange Act reports;
- issuers who are or during the prior three years were blank check companies; shell companies; penny stock issuers;
- issuers who are limited partnerships offering and selling their securities other than through a firm commitment underwriting;
- issuers who have filed for bankruptcy or insolvency during the past three years;
- issuers who have been or are the subject of refusal or stop orders under the Securities Act during the past three years, or are the subject of a pending proceeding under Securities Act Section 8 or 8A; or
- issuers who have been convicted of any felony or misdemeanor described in certain provisions of the Exchange Act, have been found to have violated the anti-fraud provisions of the federal securities laws, or have been made the subject of a judicial or administrative decree or order prohibiting certain conduct or activities

regarding the anti-fraud provisions of the federal securities laws during the past three years.

Note that a material weakness in internal control over financial reporting will not disqualify a company from taking advantage of securities offering reforms recently adopted by the SEC. Thus, under 1933 Act Rule 405, the disclosure of a material weakness will not make a company an ineligible issuer. Commenters such as KPMG and Ernst & Young had advised the SEC that companies should not be ineligible based on the disclosure of material weaknesses in internal controls over financial reporting. Until there is more experience with Section 404 reporting and the related incidence and ramifications of material weaknesses, reasoned Ernst & Young, the Commission should not condition the availability of the automatic shelf registration and offering communications safe harbors, exemptions, and exclusions on the absence of any material weaknesses as of a company's fiscal year end.

Similarly, the SEC eliminated the ineligibility condition based on a going concern opinion covering the company's most recent audited financial statements. The accounting industry had also expressed concern about this disqualification.

Communications

The Securities Act restricts the types of offering communications that issuers or other parties subject to the Act's provisions, such as underwriters, may use during a registered public offering. The nature of the restrictions depends on the period during which the communications are to occur. The restrictions do not depend on the accuracy of the information contained in the communication.

Before the registration statement is filed, all offers, in whatever form, are prohibited. Between the filing of the registration statement and its effectiveness, offers made in writing, including by e-mail or Internet, by radio, or by television are limited to a statutory prospectus that conforms to the information requirements of Securities Act Section 10. As a result, the only written material that is permitted in connection with the offering of the securities during the period between filing and effectiveness of a registration statement is a preliminary prospectus meeting the requirements of Section 10, which must be filed with the SEC.

Even after the registration statement is declared effective, offering participants still may make written offers only through a statutory prospectus, except that they may use additional written offering materials if a final prospectus that meets the requirements of Securities Act Section 10(a) is sent or given prior to or with those materials. Violations of these restrictions are referred to as "gun-jumping."

The new rules define all methods of communication, other than oral communications, as written communications for purposes of the Securities Act. The rules clarify that all electronic communications, other than telephone and other live, in real-time communications to a live audience, are graphic and, therefore, written communications.

New definitions of graphic communication and written communication have been adopted in view of the technological developments since the enactment of the Securities Act. A graphic communication will now include any form of electronic media, such as audiotapes, videotapes, facsimiles, CD-ROM, electronic mail, Internet web sites, and computers, computer networks, and other forms of computer data compilation. The definition of graphic communication does not include a communication that, at the time of the communication, originates live, in real-time, to a live audience and does not originate in recorded form or otherwise as a graphic communication.

A basic concept of the definition is that communications that are graphic communications when they are transmitted are treated as graphic communications under the definition and communications that are live, in real time communications to a live audience when they are transmitted are not treated as graphic communications.

Under the new rules, written communication means any communication that is written, printed, or television or radio broadcast (regardless of the transmission means), or a graphic communication. All communications that fall outside the definition are oral communications. The definition also excludes live telephone calls through whatever means by which they are transmitted, including the Internet, and, other live, in real-time communications to a live audience transmitted by graphic means.

The definition clarifies that television or radio broadcasts will be covered regardless of the transmission means. For example, a cable television show will be considered a television broadcast that is a written communication, and a television show or radio program that may be seen or heard through the Internet will also be considered a television or radio broadcast that is a written communication. A communication may fall outside the definition of graphic communication because it originates live, in real-time to a live audience but such communication, for example, a live business news program broadcast by traditional means or on cable, may be a television or radio broadcast. On the other hand, a live, in real-time communication that is transmitted by graphic means to a live audience would be an oral communication.

Under the new SEC definitions of graphic and written communications:

- a live telephone call is not a written communication;
- a live telephone call recorded by the recipient is not a written communication;
- e-mails, facsimiles, and electronic postings on web sites are graphic communications;
- a live, in-person road show to a live audience is not a written communication;
- a live, in real-time road show to a live audience that is transmitted graphically is not a graphic communication;
- a live, in real-time road show to a live audience that is transmitted to an overflow room is not a graphic communication;

- a webcast or video conference that originates live and in real-time at the time of transmission and is transmitted through video conferencing facilities or is webcast in real-time to a live audience is not a graphic communication;
- the ability of a member of the audience to record a webcast or video conference that is presented live and in real-time to a live audience would not affect the status of that webcast or video conference;
- a live telephone call or video or webcast conference that is recorded by the originating party and then transmitted, or is otherwise transmitted other than live and in real-time, will be a graphic communication and therefore a written communication;
- a live telephone call or video or webcast conference that is recorded by the recipient and then re-transmitted by the recipient is a graphic communication by the recipient when it is re-transmitted; and
- an interview with an issuer's chief executive officer conducted live as part of a television program is a written communication regardless of how the television signal is transmitted and regardless of how it is received by the recipient.

With respect to road shows, the SEC added a Note to Rule 433 stating that a communication that is provided or transmitted simultaneously with a road show in a manner designed to make the communication available only as part of the road show and not subsequently is deemed to be part of the road show.

The new communications rules eliminate requirements that can interrupt unnecessarily a company's normal and routine communications into the market while it is engaging in a securities offering. The new rules establish a communications framework designed to operate along a spectrum based on the type of company, its reporting history, and its equity market capitalization or recent issuances of fixed income securities. Thus, eligible well-known seasoned issuers will have freedom generally from the gun-jumping provisions to communicate at any time, including by means of a written offer other than a statutory prospectus. Varying levels of restrictions will apply to other categories of issuers.

The SEC deems these distinctions appropriate because the market has more familiarity with large, more seasoned issuers and, as a result of the ongoing market following of their activities, including the role of market participants and the media, these issuers' communications have less potential for conditioning the market for the issuers' securities to be sold in a registered offering.

The cumulative effect of the rules under the gun-jumping provisions is that:

- well-known seasoned issuers are permitted to engage at any time in oral and written communications, including use at any time of a free writing prospectus.
- all reporting issuers are permitted, at any time, to continue to publish regularly released factual business information and forward-looking information.

- non-reporting issuers are permitted, at any time, to continue to publish regularly released factual business information that is intended for use by persons other than in their capacity as investors or potential investors.
- communications by issuers more than 30 days before filing a registration statement are not prohibited offers so long as they do not reference a securities offering that is or will be the subject of a registration statement.
- all issuers and offering participants are permitted to use free writing prospectuses after the filing of the registration statement.
- a broader category of routine communications regarding issuers, offerings, and procedural matters, such as communications about the schedule for an offering or about account-opening procedures, are excluded from the definition of prospectus.
- the exemptions for research reports are expanded.

Safe Harbors

The SEC adopted two separate, non-exclusive safe harbors from the gun-jumping provisions for continuing ongoing business communications. The first safe harbor permits a reporting issuer's continued publication or dissemination of regularly released factual business and forward-looking information at any time, including around the time of a registered offering. The second safe harbor permits a non-reporting issuer's continued publication or dissemination of regularly released factual business information that is intended for use by persons other than in their capacity as investors or potential investors.

The safe harbors are not exclusive and do not create a presumption that any communication that falls outside the safe harbor is an offer. Accordingly, reliance on one of the safe harbors does not affect the availability of any other exemption or exclusion under the Securities Act. Further, attempted compliance with one of the safe harbors does not act as an exclusive election. For example, attempted reliance on one of the exemptive rules or exclusions will not preclude reliance on another available exemption or exclusion.

Communications outside of safe harbors

The SEC also adopted rules clarifying the Securities Act application to communications that might not fall within the safe harbors for regularly released factual business and forward-looking information. New Rule 163A provides all issuers a bright-line time period, ending 30 days prior to filing a registration statement, during which they may communicate without risk of violating the gun-jumping provisions. Such communications will be excluded from the definition of offer for purposes of Securities Act Section 5(c).

A 30-day timeframe was chosen because it is consistent with the timeframe in Securities Act Rule 155 regarding the integration of abandoned offerings, as well as Rule 254 regarding pre-filing solicitations of interest in Regulation A offerings.

As adopted, the 30-day bright-line exclusion from the gun-jumping provisions is subject to the following conditions:

- a communication made in reliance on the Rule cannot reference a securities offering that is or will be the subject of a registration statement;
- a communication made in reliance on the Rule will have to be made by or on behalf of the issuer; and
- the issuer will have to take reasonable steps within its control to prevent further distribution or publication of the communication during the 30-day period immediately before it files the registration statement.

The Rule is designed to preclude issuers and offering participants from circumventing the registration requirements of the Securities Act. Because the Rule does not permit information about a securities offering that is or will be the subject of a registration statement, the communications made in reliance on the Rule are less likely to be used to condition the market for the issuer's securities.

Communications made in reliance on the Rule 163A safe harbor also would not be made in connection with a registered securities offering for purposes of the exclusion in Regulation FD. See Rule 100(b)(2)(iv) of Regulation FD.

The 30-day bright-line exclusion is not available for enumerated categories of offerings and for specified issuers that pose the greatest risk of abuse of that exclusion. Specifically, Rule 163A is not available to communications made in connection with offerings by a blank check company; offerings by a shell company; or offerings of penny stock by an issuer.

The Rule also excludes communications regarding business combination transactions from being able to rely on the exclusion, as those communications are regulated separately. The Rule also is not available for communications regarding offerings made by a registered investment company or a business development company.

The rules also expand the amount and types of permitted written offering-related communications that may be made by offering participants under the gun-jumping provisions after a registration statement is filed. The two main elements of these rules are expansion of information that Securities Act Rule 134 permits to be communicated and the permitted use of free writing prospectuses in connection with a registered offering.

Rule 134 provides a safe harbor from the gun-jumping provisions for limited public notices about an offering made after an issuer files its registration statement. The Rule was intended originally to provide an identifying statement that could be used to locate persons that might be interested in receiving a prospectus. All issuers, including well-known seasoned issuers, are precluded from relying on Rule 134 until the issuer files a registration statement that includes a statutory prospectus.

The SEC has modified and expanded the information permitted under Rule 134 to include information that issuers, underwriters, and investors will find helpful and to permit the types of written communications during an offering that do not raise the risk of offering abuses. The amendments to Rule 134 will:

- permit increased information about an issuer and its business, including where to contact the issuer;
- permit more information about the terms of the securities being offered;
- expand the scope of permissible factual information about the offering itself, including underwriter information, more details about the mechanics of and procedures for transactions in connection with the offering process, the anticipated schedule of the offering, and a description of marketing events;
- allow more factual information about procedures for account opening and submitting indications of interest and conditional offers to buy the offered securities;
- allow more factual information regarding procedures for directed share plans and other participation in offerings by officers, directors, and employees;
- permit the correction of inaccuracies in permissible information previously disclosed pursuant to the Rule; and
- expand the disclosure permitted regarding credit ratings to include the security rating that is reasonably expected to be assigned.

The information on marketing events, such as road shows, can include greater detail on the date, time, location, and procedures for attending or otherwise accessing the events.

Note that the expansion does not permit use of a Rule 134 notice to provide a detailed description of securities being offered. There is increased ability under SEC rules, however, to provide such a detailed description, such as a term sheet, as a free writing prospectus.

The SEC also modified the information that must be included in a Rule 134 notice. For example, the reference in the legend to state securities laws has been eliminated since other provisions of the Rule already address any state securities law requirements. Also eliminated was the requirement to specify whether the financing is a new financing or refunding.

While Rule 134 does not embody the principle of access equals delivery, the SEC will now allow persons providing notices relying on Rule 134 to include a URL address to the statutory prospectus that alerts investors where they can obtain a statutory prospectus. For purposes of Rule 134, including a URL address to the statutory prospectus that is not an active hyperlink in an electronic communication does not mean that the prospectus has been delivered. An active hyperlink to a statutory prospectus in an electronic Rule 134 notice, however, will satisfy the requirement that the prospectus accompany or precede that notice.

Free Writing Prospectuses

After the filing of a registration statement, the gun-jumping provisions permit issuers to make written offers only in the form of a statutory prospectus. After effectiveness of a registration statement, written offers other than a statutory prospectus may be made only if a final prospectus meeting the requirements of Securities Act Section 10(a) is sent or given prior to or at the same time as the written offer.

The SEC has adopted rules permitting written offers, including electronic communications, outside the statutory prospectus beyond those currently permitted by the Securities Act, if certain conditions are met. Such a written offer outside of the statutory prospectus will be known as a free writing prospectus. A free writing prospectus can be used by a well-known seasoned issuer at any time.

The SEC defines a free writing prospectus as a written communication that constitutes an offer to sell or a solicitation of an offer to buy securities that are or will be the subject of a registration statement and is not:

- a prospectus satisfying the requirements of Securities Act Section 10(a);
- a prospectus satisfying rules permitting the use of preliminary or summary prospectuses or prospectuses subject to completion;
- a communication made in reliance on the special rules for asset-backed issuers permitting the use of ABS informational and computational materials; or
- a prospectus because a final prospectus meeting the requirements of Section 10(a) was sent or given with or prior to the written communication.

The definition clarifies that, although a free writing prospectus will not be filed as part of a registration statement, it will still be considered to relate to a registered public offering of securities that is or will be the subject of a registration statement, regardless of the method of its use or distribution. Further, a written communication will be a free writing prospectus only where it constitutes an offer by an offering participant of a security under the Securities Act. Whether a particular communication constitutes such an offer will continue to be determined based on the particular facts and circumstances.

While the definition of offer is broad under the federal securities laws, not all communications relating to an offering are offers or offers by an offering participant. As a non-exclusive illustration, the gun-jumping provisions have been administered in a manner that excludes from categorization as an offer a media publication or television or radio broadcast that is based solely on information that is filed with the SEC or available on an unrestricted basis or on other information the dissemination of which did not represent an offer by an issuer or other offering participant, where there is no other involvement or participation by an offering participant.

On that basis, for example, a newspaper article about an initial public offering that is based on the filed registration statement, on a press release that is filed with or furnished to the SEC, on a filed free writing prospectus, or on filed issuer information where the

issuer and other offering participants have refused to comment and not otherwise been involved, would not be categorized as an offer under the gun-jumping provisions.

The SEC decided not to include any specific provision in the new rules regarding offshore communications. Thus, the treatment of offshore communications under the free writing prospectus rules will be no different than the treatment of any offshore communication prior to the new rules. Whether an offshore communication is considered an offer in the United States subject to the federal securities laws will still depend on when and how the communication is made and the availability of other exemptions, such as those for offshore press conferences.

For any offering participant to use free writing prospectuses, other than free writing prospectuses that consist only of descriptions of the securities in the offering or of the offering, the issuer may not be an ineligible issuer. The SEC modified the consequences of ineligibility in the context of use of free writing prospectuses to permit ineligible issuers, other than blank check companies, shell companies, and penny stock issuers, to use free writing prospectuses that are limited to descriptions of the terms of the securities being offered and the offering based on the belief that the permitted use of such free writing prospectuses can provide advantages to investors that justify the risks of use of such materials by some classes of ineligible issuers.

Ineligible issuers

Under the SEC rules, ineligible issuers are:

- reporting issuers who are not current in their Exchange Act reports;
- issuers who are or during the prior three years were blank check companies; shell companies; penny stock issuers;
- issuers who are limited partnerships offering and selling their securities other than through a firm commitment underwriting;
- issuers who have filed for bankruptcy or insolvency during the past three years;
- issuers who have been or are the subject of refusal or stop orders under the Securities Act during the past three years, or are the subject of a pending proceeding under Securities Act Section 8 or 8A; or
- issuers who have been convicted of any felony or misdemeanor described in certain provisions of the Exchange Act, have been found to have violated the anti-fraud provisions of the federal securities laws, or have been made the subject of a judicial or administrative decree or order prohibiting certain conduct or activities regarding the anti-fraud provisions of the federal securities laws during the past three years.

Note that a material weakness in internal control over financial reporting will not disqualify a company from taking advantage of securities offering reforms recently adopted by the SEC. Thus, under 1933 Act Rule 405, the disclosure of a material

weakness will not make a company an ineligible issuer. Commenters such as KPMG and Ernst & Young had advised the SEC that companies should not be ineligible based on the disclosure of material weaknesses in internal controls over financial reporting. Until there is more experience with Section 404 reporting and the related incidence and ramifications of material weaknesses, reasoned Ernst & Young, the Commission should not condition the availability of the automatic shelf registration and offering communications safe harbors, exemptions, and exclusions on the absence of any material weaknesses as of a company's fiscal year end.

Similarly, the SEC eliminated the ineligibility condition based on a going concern opinion covering the company's most recent audited financial statements. The accounting industry had also expressed concern about this disqualification.

After the filing of a registration statement, a free writing prospectus that meets the requirements of Rule 164 and satisfies the conditions of Rule 433 will be a permitted prospectus under Section 10(b) for purposes of Securities Act Section 5(b)(1). The Rule 433 conditions on the use of free writing prospectuses relate to:

- the delivery or availability of the statutory prospectus at the time the free writing prospectus is used;
- the information contained in the free writing prospectus;
- the legend that is to be included in the free writing prospectus;
- filing of the free writing prospectus; and
- record retention for the free writing prospectus.

Prospectus delivery or availability

The ability of any person participating in the offer and sale of the securities to use free writing prospectuses under Rules 164 and 433 generally is conditioned on the filing of a registration statement that includes a prospectus satisfying the requirements of Securities Act Section 10. Further, in specified cases, Rule 433 conditions the use of a free writing prospectus on prior or concurrent delivery of the issuer's most recently filed statutory prospectus.

In an offering of securities of an eligible non-reporting issuer, including an initial public offering, or securities of an eligible unseasoned issuer, the use by an offering participant of free writing prospectuses is conditioned on: (1) filing of the registration statement for the offering; and (2) the free writing prospectus being preceded or accompanied by the most recent statutory prospectus that satisfies the requirements of Section 10.

Issuers and offering participants must assure that the most recent statutory prospectus is actually provided to anyone who might receive a free writing prospectus. Thus, in the SEC's view, the use of broadly disseminated free writing prospectuses in registered offerings by these types of issuers and offering participants in these offerings may not be

feasible unless they are in electronic form and contain a hyperlink to the statutory prospectus.

The condition that the statutory prospectus precede or accompany the free writing prospectus will not require that it be provided through the same means, so long as it is provided at the required time. Further, referring to its availability will not satisfy this condition.

In the following situations, for example, the most recent statutory prospectus must precede or accompany the free writing prospectus or the communication cannot be made in reliance on Rules 164 and 433:

- a direct written communication by an issuer or offering participant;
- a written communication or a television or radio broadcast prepared by or on behalf of or used or referred to by an issuer or an offering participant;
- the dissemination, in any format including publication or broadcast, of any free writing prospectus (including any published article, publication, or advertisement) for which consideration is or will be given by the issuer or an offering participant; or
- a paid published or broadcast advertisement by an issuer or offering participant.

Once the required statutory prospectus is provided to an investor, additional free writing prospectuses can be provided to that investor without having to provide an additional statutory prospectus, unless there is a material change in the most recent statutory prospectus from the provided prospectus. For example, once an investor has been sent a preliminary prospectus, absent a material change, the rules permit subsequent e-mail communications to that investor by an offering participant that constitute free writing prospectuses without the user having to hyperlink to or otherwise redeliver a statutory prospectus with each communication.

After effectiveness and availability of a final prospectus meeting the requirements of Securities Act Section 10(a), no earlier statutory prospectus may be provided, and such final prospectus, as revised or supplemented, must precede or accompany any free writing prospectus provided after such availability, whether or not an earlier statutory prospectus has been previously provided to the recipient.

Prospectus availability condition for seasoned and well-known seasoned issuers

In offerings of securities of eligible seasoned issuers and eligible well-known seasoned issuers, a free writing prospectus may be used after the filing of a registration statement containing a statutory prospectus. For shelf offerings, this statutory prospectus can be base prospectus.

For offerings of securities of eligible seasoned and well-known seasoned issuers, the rules do not condition use of the free writing prospectus on actual delivery of the most recent statutory prospectus. Instead, the user of the free writing prospectus must notify

the recipient, through a required legend, of the filing of the registration statement and the URL where the recipient can access or hyperlink to the preliminary or base prospectus. The rules permit the use of a generic rather than an issuer-specific legend. The legend must contain a toll-free telephone number, and may contain an e-mail address, through which the statutory prospectus may be requested.

In the event that a well-known seasoned issuer does not have a registration statement on file, Rule 163 provides that an eligible well-known seasoned issuer's written offers are exempt from Section 5(c). While it will be exempt from the requirements of Section 5(c), a written offer made under the exemption in Rule 163 will fall within the definition of free writing prospectus.

Information condition

The rules allow information in a free writing prospectus to go beyond information the substance of which is contained in the prospectus included in the registration statement. However, the information in the free writing prospectus must not conflict with the information in the registration statement, including Exchange Act reports incorporated by reference into the registration statement.

Investor protection remains undiminished, the SEC believes, because the liability provisions applicable to free writing prospectuses, particularly Securities Act Section 12(a)(2) and the anti-fraud provisions of the federal securities laws, provide protection against material misstatements in, and material omissions from, information contained in such free writing prospectus.

Note that information in the free writing prospectus may be different from or additional or supplemental to that in the registration statement, so long as it does not conflict with the latter. Further, free writing prospectuses may incorporate or refer investors to other information, so that investors will be advised to consider the information presented in the free writing prospectus in context. In addition, the legend that must be included in a free writing prospectus will direct investors to the filed prospectus contained in the registration statement.

A free writing prospectus cannot include language that deems an investor to have read or have knowledge of other documents incorporated in or referred to in the free writing prospectus. Whether such other information is conveyed to the investor will be determined based on the facts and circumstances.

A further protection is that the SEC retains the ability to halt the use of any materially false or misleading free writing prospectus in accordance with the antifraud provisions. The SEC staff will be able to request any free writing prospectus that has been used in connection with a securities offering.

Rule 408 clarifies that not including information that is included in a free writing prospectus in a prospectus filed as part of a registration statement will not, solely by virtue of inclusion of the information in a free writing prospectus, be considered an omission of material information required to be included in the registration statement.

The use of a free writing prospectus is conditioned on the inclusion of a legend indicating where a prospectus is available for the offering to which the communication relates and recommending that potential investors read the prospectus. The legend also advises investors that they can obtain the registration statement including the prospectus and any incorporated Exchange Act documents for free at www.sec.gov, and that they may request the prospectus from the issuer, any underwriter or any dealer by calling a toll-free number. The legend also indicates that the free writing prospectus relates to a registered public offering. The SEC mandates a generic, rather than an issuer-specific legend, in order to assist issuers in including a legend in a free writing prospectus without much added cost.

The legend condition is intended to more clearly identify materials as free writing prospectuses used in relation to a registered offering. The SEC believes that this legend will put investors on notice and assist them in evaluating the content of the free writing prospectus.

An unintentional or immaterial failure to include the legend in any free writing prospectus can be cured so long as a good faith and reasonable effort is made to comply with the condition and the free writing prospectus is amended to include the legend as soon as practicable after discovery of the omission. In addition, if a free writing prospectus has been transmitted to potential investors without the legend, the free writing prospectus must be retransmitted with the appropriate legend and by substantially the same means as and directed to substantially the same investors to whom it was originally transmitted.

Issuers may sometimes include legends or disclaimers in offering materials that may be inappropriate. In particular, disclaimers of responsibility or liability that are impermissible in a statutory prospectus or registration statement are also impermissible in free writing prospectuses. The following are non-exclusive examples of impermissible legends or disclaimers that will cause the materials not to be permissible free writing prospectuses or not to be effective as to any purchaser for liability purposes:

- disclaimers regarding accuracy or completeness or reliance by investors;
- statements requiring investors to read or acknowledge that they have read or understand the registration statement or any disclaimers or legends;
- language indicating that the communication is neither a prospectus nor an offer to sell or a solicitation or an offer to buy; and
- for information that must be filed with the SEC, statements that the information is confidential.

Filing conditions

Use of a free writing prospectus is also conditioned on the filing of that prospectus or information contained in it, unless exempt from filing, in the following circumstances:

- The issuer must file a free writing prospectus that it prepares or uses or refers to, known as an issuer free writing prospectus;
- Where a free writing prospectus prepared by or used by an offering participant other than the issuer contains issuer information that is not already included or incorporated in the prospectus or a filed free writing prospectus, the issuer must file the issuer information;
- An offering participant must file a free writing prospectus that it uses or refers to and that is distributed in a manner reasonably designed to lead to its broad unrestricted dissemination; and
- where a free writing prospectus prepared by the issuer or other offering participant comprises a description of the final terms of the issuer's securities in the offering or of the offering, the issuer must file such free writing prospectus after such terms have been established for all classes of the offering.

In most cases, there is no condition that underwriters and dealers file the free writing prospectuses that they prepare, use, or refer to. This includes information prepared by underwriters and others on the basis of or derived from, but not containing, issuer information. Such information can be, but is not limited to, information that is proprietary to the preparer.

Under Rule 433, electronic road shows that are written communications are not subject to the filing condition in certain circumstances.

Rule 164 provides an issuer the ability to cure any immaterial or unintentional failure to file or delay in filing the free writing prospectus. This cure provision is available if a good faith and reasonable effort is made to comply with the filing condition and the free writing prospectus is filed as soon as practicable after the discovery of the failure to file.

Record retention condition

The use of a free writing prospectus is further conditioned on issuers and offering participants retaining for three years any free writing prospectuses they have used from the date of the initial bona fide offering of the securities in question that have not been filed with the SEC. Note that this record retention condition applies to all offering participants; and that the three-year retention period is consistent with retention periods for brokers and dealers to retain securities sale confirmations.

While there is no cure provision for failure to retain free writing prospectuses, Rule 164 provides that an immaterial or unintentional failure to retain a free writing prospectus will not result in a violation of Securities Act Section 5(b)(1) or the loss of the ability to rely on the exemption so long as a good faith and reasonable effort was made to comply with the record retention condition.

Road Shows

Issuers and underwriters frequently conduct presentations known as road shows to market their offerings to the public. As primary means by which issuers are involved directly and actively in a selling effort to investors, road shows were historically conducted in person and limited to institutional investors. Today, road shows are also conducted or re-transmitted over the Internet or other electronic media and in some cases to broader audiences.

The SEC has excluded from the definition of graphic communication a communication that originates live, in real-time to a live audience and does not originate in recorded form or otherwise as a graphic communication, although it may be transmitted through graphic means. Thus, a live, in real-time road show to a live audience that is transmitted graphically will not be a graphic communication, and therefore not a written communication, or a free writing prospectus. It will still, however, be an offer subject to Securities Act Section 12(a)(2) and the other liability provisions of the federal securities laws.

It follows that information presented as part of the live, in real-time road show to a live audience will not be a free writing prospectus. Slides or other visual aides transmitted simultaneously as part of a live road show that is not a written communication, and provided or transmitted in a manner designed to make it available only as part of the road show and not separately, are deemed to be part of the road show and not a written communication.

In-person road shows will continue to be considered oral communications. And, the exclusion for presentations to a live audience that originate live, in real-time also covers overflow rooms at live, in-person road shows. The rules do not affect the treatment of written communications or road shows regarding business combination transactions to which Rule 425 and Regulation M-A apply.

While the SEC has revised the definition of graphic communication to exclude certain presentations that originate live, in real-time to a live audience, the Commission has retained in the definition of written communications the statutory concept of radio or television broadcasts, regardless of the transmission means. Thus, a communication that is a television or radio broadcast, whether or not live, would still be a written communication.

Road shows that do not originate live, in real-time to a live audience and are graphically transmitted are electronic road shows that will be considered written communications and, therefore, free writing prospectuses. They are permitted if the conditions of the new rules for free writing prospectuses are satisfied. Issuer involvement or participation in an electronic road show that is a written communication will make it an issuer free writing prospectus.

The SEC recognizes that road shows may also be used in marketing the issuer's securities in certain private placement transactions. The rules do not address these offerings, although the treatment of electronic communications in the definitions of graphic communication and written communication apply to private placement transactions. For example, in an offering made in reliance on Securities Act Rule 505 or Rule 506 of Regulation D, an electronic road show or other communication that is a

written communication would implicate the provisions of Rule 502 regarding information that must be provided to non-accredited investors and restrictions on general solicitation and general advertising.

Up until now, electronic road shows have proceeded in reliance on a series of no-action letters granted by the SEC's Division of Corporation Finance. Since the new rules permit the use of electronic road shows without many of the conditions in the electronic road show no-action letters, the no-action letters have been withdrawn.

Under the new rules, audiences at road shows that are free writing prospectuses do not have to be limited in any way, and the road show does not have to be the re-transmission of a live presentation in front of an audience and the electronic road show may be edited. In addition, those distributing the road show do not have to limit viewers to seeing it either within a 24-hour period or twice. They also can allow viewers to copy, print or download the road show. Multiple versions of the electronic road show are permitted. Each will be a separate free writing prospectus.

The SEC defines a road show to be an offer, other than a statutory prospectus, that contains a presentation regarding an offering by one or more members of the issuer's management and includes discussion of one or more of the issuer, such management, and the securities being offered. In the case of asset-backed offerings, road shows can include presentations by management involved in the securitization or servicing by the depositor, sponsor, or servicers.

A bona fide electronic road show is defined as a road show that is a written communication transmitted by graphic means containing a presentation by issuer management and, if the issuer is using or conducting more than one road show that is a written communication, includes discussion of the same general areas of information regarding the issuer, such management, and the securities being offered as such other issuer road shows for the same offering that are written communications. To be bona fide, the version need not address all of the same subjects or provide the same information as the other versions of an electronic road show. It also need not provide an opportunity for questions and answers or other interaction, even if other versions of the electronic road show do provide such opportunities.

It is important to remember that the bona fide version must only cover the same general areas regarding the issuer, its management, and the securities being offered and need not address all the same subjects or provide the same information as other versions.

Generally, there is no obligation to file any material issuer information provided at an electronic road show. Further, slides or visual aids provided with a live road show designed to make them available only as part of the road show and not separately are deemed to be part of the road show. Thus, if the road show is not a written communication, such slides and graphs are not deemed to be written even if they would otherwise be a graphic or written communication.

This provision would cover, for example, a communication of visual aids provided in a separate feed from a live, in real-time road show to a live audience transmitted by graphic means, where the separate communication is provided or transmitted in a manner

such that it can only be seen as part of the road show. If the road show is written and not required to be filed, such a simultaneous communication is also not required to be filed. Also covered are visual aids transmitted in a manner designed to make them available simultaneously only as part of an electronic road show. If the electronic road show is not subject to filing, neither are the visual aids. Otherwise, graphic or other written communications provided separately, for example by graphic means in a separate file designed to be available to be copied or downloaded separately, will be treated as a written communication and, if an offer, will be a free writing prospectus.

Whether written communications or not, all road shows that are offers are subject to Securities Act Section 12(a)(2) liability. In addition, all road shows that are offers that are written communications are free writing prospectuses, whether or not required to be filed.

The SEC believes that the new regime for road shows strikes the appropriate balance between the need to market an issuer's securities to institutional investors and the desires of retail and other investors to have access to issuer information, such as management presentations, that are normally available only at road shows that have often not been open to retail investors generally.

While not requiring that road shows be made available to unrestricted audiences, the SEC urged issuers and underwriters to make road shows available to all investors. Indeed, the new rules encourage issuers to do so where retail interest justifies such unrestricted availability.

Electronic Communications

The new communications rules are designed to enable issuers and market participants to take significantly greater advantage of the Internet and other electronic media to communicate and deliver information to investors. Specifically, there will now be an ability to communicate outside the statutory prospectus, including posting information on web sites that will be free writing prospectuses.

For example, under Rule 433(e), an offer of an issuer's securities that is contained on its web site, or on a third-party web site hyperlinked from the issuer's web site, is considered a written offer of such securities made by the issuer and, unless otherwise exempt, will be a free writing prospectus of the issuer. However, an exception in Rule 433(e)(2) provides that historical information will not be considered a current offer of the issuer's securities and, therefore, will not be a free writing prospectus, if that historical information is: (1) separately identified as such; and (2) located in a separate section of the web site containing such information.

Note also that the use of that historical information will become a current offer if it is incorporated by reference into or otherwise included in a prospectus of the issuer for the offering or otherwise used or referred to in connection with the offering.

While Rule 433(e)(2) addresses particular situations in which information retained on a web site will not be considered a free writing prospectus, other information located on or hyperlinked to a web site might similarly not be considered a current offer of the

issuer's securities and, therefore, not a free writing prospectus, where it can be shown that the information was published previously. For example, certain information that, while not contained in a separate section of an issuer's web site, is dated or otherwise identified as historical information and is not referred to in connection with the offering activities may not be a current offer, depending on the particular facts and circumstances.

Media Publications

The SEC encourages the role of the media as an important communicator of information and some media publications regarding an offering are not categorized as offers, under the gun-jumping provisions, by issuers or other offering participants. However, the Commission does not want issuers and offering participants to avoid responsibility for their offering or marketing efforts by using the media. This is why the new rules address offers that take place using the media as a communication vehicle.

The rules provide that, where an issuer or any offering participant provides information about the issuer or the offering that constitutes an offer, whether orally or in writing, to a member of the media and where the media publication of that information is an offer by the issuer or other offering participant, the SEC will consider the publication to be a free writing prospectus of the issuer or offering participant in question.

The treatment of a media publication that constitutes an offer, and therefore a free writing prospectus of the issuer, will depend on whether the issuer prepares the publication or television or radio broadcast or pays for or provides other consideration for the publication or broadcast, or whether unaffiliated media prepares and publishes or broadcasts the communication for no consideration or payment from an issuer or offering participant.

If an issuer prepares or pays for the preparation, publication or dissemination of, or uses or refers to, a published article, television or radio broadcast, or advertisement, the issuer will have to satisfy the conditions to the use of any other free writing prospectus of that offering participant at the time of the publication or broadcast. For example, in the case of a non-reporting issuer or reporting unseasoned issuer, a statutory prospectus will have to precede or accompany the communication. As a consequence of this requirement, in offerings by non-reporting and unseasoned issuers, issuers and offering participants will not be able to prepare or pay for published or broadcast written advertisements, infomercials, or broadcast spots or similar written communications about the issuer, its securities, or the offering that includes information beyond that permitted by Rule 134.

Well-known seasoned and other seasoned issuers and offering participants will have to comply with the other applicable conditions for the free writing prospectus. For seasoned issuers that are not well-known seasoned issuers and offering participants, a registration statement including a statutory prospectus will have to be on file with the SEC.

However, the rules can be accommodating when the free writing prospectus is prepared and published or broadcast by persons in the media business that are unaffiliated with the issuer and the preparation, publication, or broadcast is not paid for by the issuer

or an offering participant. In these cases, an issuer would not have to have a statutory prospectus precede or accompany the media communication, although a filed registration statement including a statutory prospectus would be necessary, except in the case of a well-known seasoned issuer. Therefore, an interview or other media publication or television or radio broadcast where an issuer or offering participant participates, but does not prepare or pay for the event or article, could be a free writing prospectus. But because of the media intervention, the SEC concluded that its use should not be conditioned on prior or simultaneous delivery of the statutory prospectus.

For example, an underwriter or issuer will be permitted to invite the press to a live road show or an electronic road show, but, in most cases, the SEC will consider an article including information obtained at that road show to be a free writing prospectus of the issuer or underwriter and subject to the rules regarding free writing prospectuses. Further, assuming that the road show in question is an offer, an article published based on information obtained from a road show with a limited audience could be a free writing prospectus depending on its content. An article published based solely on information provided at a readily accessible electronic road show open to an unrestricted audience may not be an offer where there is no other involvement by an issuer or offering participant.

The filing condition of Rule 433(d) will be satisfied where a free writing prospectus including information about the issuer, its securities, or the offering provided, authorized, or approved by the issuer, and that is prepared and published or disseminated by persons in the media business who are not affiliated with or paid by the issuer, is filed by the issuer within four business days after becoming aware of its publication or first broadcast. Note that persons in the media have no filing or other responsibilities under these provisions.

Issuers can satisfy the filing condition by filing: (1) the media publication; (2) all of the information provided to the media in lieu of the publication; or (3) a transcript of the interview or similar materials that the issuer or other offering participant provided to the media so long as all the information provided is filed.

In addition, the issuer does not have to file the media publication if the substance of the written communication has been previously filed with the SEC. Moreover, the issuer may file, together with or after the media publication is filed, information that the issuer reasonably believes is necessary or appropriate to correct information included in the media publication.

Finally, a limited exclusion would permit issuers that are in the media business to be able to rely on the unaffiliated media condition if the media issuer or its affiliated media business:

- is the publisher of a bona fide newspaper, magazine, or business or financial publication of general and regular circulation or bona fide broadcaster of news including business and financial news;
- has established policies and procedures for the independence of the content of the publication or broadcast from the offering activities; and

- publishes or broadcasts the communication in the ordinary course.

Interaction with Regulation FD

As a consequence of the new rules liberalizing communications during the offering process and encouraging ongoing regular communications by reporting issuers, the SEC revised the exclusions from Regulation FD for communications made during a registered offering of securities. The new communications regime contemplates that, in connection with an offering, certain material inside information can be made public through the prospectus filed as part of a registration statement or the issuer's filing of a free writing prospectus.

A company's oral communications made in connection with a registered offering after the registration statement is filed will continue not to be subject to any filing or public disclosure requirement.

The Commission revised Regulation FD to specify the circumstances, both in terms of the type of offering and the means of communication, in which issuer communications will be excluded from its operation in connection with a registered securities offering. Regulation FD will not apply to disclosures made in the following communications in connection with a registered securities offering that is of the type excluded from the regulation:

- a registration statement filed under the Securities Act, including a prospectus contained in it;
- a free writing prospectus used after filing of the registration statement for the offering or a communication excepted from the definition of prospectus ;
- any other Section 10(b) prospectus;
- a notice permitted by Securities Act Rule 135;
- a communication permitted by Securities Act Rule 134; or
- an oral communication made in connection with the registered securities offering after filing of the registration statement for the offering under the Securities Act.

In addition, Regulation FD will not apply to offerings by selling shareholders where the offering also includes a registered offering, whether or not underwritten, for capital formation purposes for the account of the issuer, so long as the issuer's offering is not included for the purpose of evading Regulation FD. The amendments do not otherwise change the types of registered offerings that are excluded from, or subject to, the operation of the Regulation.

It is important to remember that the communications excluded from the operation of Regulation FD are those that are directly related to a registered securities offering. Communications not contained in the enumerated list of exceptions from Regulation FD, for example, the publication of regularly released factual business information or

regularly released forward-looking information or pre-filing communications, are subject to Regulation FD.

In addition, the change to Regulation FD does not mandate that all registered securities offerings be for capital formation purposes as a condition of exclusion from the operation of Regulation FD. The exclusions prior to and after the change have the general effect of excluding capital formation transactions, but there was, and after the change there will be, no separate capital formation requirement for the exclusions. Rather, the change provides that secondary offerings will be excluded from Regulation FD if the offerings also include a registered capital formation transaction for the account of the issuer.

Research Reports

The value of research reports in continuing to provide the market and investors with information about reporting issuers is undisputed. Thus, the SEC limited the restrictions on research under the gun-jumping provisions of the Securities Act to those appropriate to avoid offering abuses. Given the ongoing flow of information into the market, particularly with respect to reporting issuers and the enhancements to the environment for research imposed by recent developments, the SEC effected measured revisions to the research rules that, while consistent with investor protection, will also permit dissemination of research around the time of an offering under a broader range of circumstances.

Rules 137, 138, and 139 under the Securities Act describe circumstances in which a broker or dealer may publish research constituting an offer around the time of a registered offering without violating the Section 5 prohibitions on pre-filing offers and impermissible prospectuses. The SEC has amended the rules to expand the circumstances in which offering participants and persons who are not offering participants will have safe harbor exemptions for dissemination of research reports during a registered offering. In addition, for the first time, research report is defined.

The safe harbor provisions of Securities Act Rules 137, 138, and 139 will continue to be available only to brokers and dealers. Issuers cannot use the safe harbor provisions for research reports prepared or distributed by brokers or dealers in reliance on the rules to communicate with potential investors about the issuer's offering. For example, a hyperlink to a research report on an issuer's web site during its registered offering could raise concerns in this regard. Issuers using research reports in this manner could be deemed to have adopted the contents of such reports and the reports could be considered free writing prospectuses.

In addition, the rules will continue to permit the distribution of independent research within the safe harbors. For brokers and dealers subject to the global research analyst settlement, their ability to continue to distribute independent research during a registered securities offering depends on concluding that the independent research distribution by the broker or dealer satisfies the conditions of the research rule at the time of the distribution or is otherwise not an offer. If a broker or dealer is not able to rely on any of

the research safe harbors for their own research, they similarly cannot rely on the safe harbor to distribute independent research.

The rules define a research report as a written communication that includes information, opinions, or recommendations with respect to securities of an issuer or an analysis of a security or an issuer, whether or not it provides information reasonably sufficient upon which to base an investment decision. The definition is intended to encompass all types of research reports, whether issuer-specific or industry research separately identifying the issuer.

Liability Issues

Even when filed, a free writing prospectus will not be part of a registration statement subject to liability under Securities Act Section 11, unless the issuer elects to file it as a part of the registration statement. Regardless of whether a free writing prospectus is filed, any seller offering or selling securities by means of the free writing prospectus will be subject to disclosure liability under Securities Act Section 12(a)(2). A free writing prospectus can also be the basis for liability under the anti-fraud provisions of the federal securities laws.

A free writing prospectus used after a registration statement is filed complying with Rule 433 will be governed by the provisions of Securities Act Section 10(b), which provides that a prospectus permitted under that section is filed as part of the registration statement, but is not subject to Section 11 liability. The SEC modified the Section 10(b) filing requirement to provide that a free writing prospectus filed pursuant to Rule 433 must identify the registration statement to which it relates, but Rule 433 provides that it will not have to be filed as part of the registration statement.

Sections 12(a)(2) and 17(a)(2)

Under the Securities Act, purchasers of an issuer's securities in a registered offering have private rights of action for materially deficient disclosure in registration statements under Section 11 and in prospectuses and oral communications under Section 12(a)(2). Section 11 liability exists for untrue statements of material facts or omissions of material facts required to be included in a registration statement or necessary to make the statements in the registration statement not misleading at the time the registration statement became effective.

Under Section 12(a)(2), sellers have liability to purchasers for offers or sales by means of a prospectus or oral communication that includes an untrue statement of material fact or omits to state a material fact that makes the statements made, based on the circumstances under which they were made, not misleading. Securities Act Section 17(a) is a general anti-fraud provision that provides, among other things, that it shall be unlawful for any person in the offer and sale of a security to obtain money or property by means of any untrue statement of a material fact or any omission to state a material fact

necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading.

The term "sale" under the Securities Act includes any contract of sale. The SEC has addressed the discrepancies in time between the time of the contract of sale for securities, when an investor becomes committed to purchase the securities, on the one hand, and the later time of availability of a prospectus and perhaps other information on the other hand. The Securities Act registration regime permits final prospectuses to become available after an investor becomes committed to purchase a security. This availability, therefore, does not necessarily address the receipt by an investor of information at the time of its contractual commitment.

Under the SEC's interpretation, Sections 12(a)(2) and 17(a)(2) do not require that oral statements or the prospectus or other communications contain all information called for under the line-item disclosure rules or otherwise contain all material information. Rather, under these provisions, the determination of liability is based on whether the communication includes a material misstatement or fails to include material information that is necessary to make the communication, under the circumstances in which it is made, not misleading. Thus, the time at which an investor has taken the action the investor must take to become committed to purchase the securities, and has therefore entered into a contract of sale, is one appropriate time to apply the liability standards.

The SEC interprets Sections 12(a)(2) and 17(a)(2) as meaning that, for purposes of assessing whether at the time of sale a prospectus or oral communication or statement includes a material misstatement or omits to state a material fact necessary in order to make the prospectus, oral communication, or statement not misleading, information conveyed to the investor only after the time of sale should not be taken into account. For purposes of the two statutes, whether or not information has been conveyed to an investor at or prior to the time of the contract of sale currently is a facts and circumstances determination and will remain so.

The SEC saw an uncertainty as to issuer liability under Section 12(a)(2) for issuer information in registered offerings using certain types of underwriting arrangements. As a result, there is a possibility that issuers may not be held liable under Section 12(a)(2) to purchasers in the initial distribution of the securities for information contained in the issuer's prospectus included in its registration statement. This also could be the case for other communications that are offers by or on behalf of an issuer, including issuer free writing prospectuses.

When an issuer registers securities to be sold in a primary offering, the registration covers the offer and sale of its securities to the public. The issuer is selling its securities to the public, although the form of underwriting of such offering, such as a firm commitment underwriting, may involve the sale first by the issuer to the underwriter and then the sale by the underwriter to the public. The SEC believes that an issuer offering or selling its securities in an offering pursuant to a registration statement containing a prospectus that it has prepared and filed, or by means of other communications that are offers made by the issuer, can be viewed as soliciting purchases of the issuer's registered securities.

Therefore, the SEC adopted a rule providing that, under Section 12(a)(2), an issuer in a primary offering of securities, regardless of the form of the underwriting arrangement, will be a seller and will be considered to offer or sell the securities to a purchaser in the initial distribution of the securities as to any of the following communications:

- any preliminary prospectus or prospectus of the issuer relating to the offering required to be filed pursuant to Securities Act Rule 424 or Rule 497;
- any free writing prospectus relating to the offering prepared by the issuer;
- the portion of any other free writing prospectus relating to the offering containing material information about the issuer or its securities provided by or on behalf of the issuer; and
- any other communication that is an offer in the offering made by the issuer to such purchaser.

This definition of the issuer as a seller is not intended to affect whether any other person offers or sells a security by means of the same prospectus or oral communication for purposes of Section 12(a)(2). A communication by an underwriter or dealer participating in an offering would also not be on behalf of the issuer solely by virtue of that participation.

Shelf Registration

The SEC revised the operation of the shelf registration system under the Securities Act. The new provisions:

- codify the information to be included in and omitted from base prospectuses in shelf registration statements;
- codify the manner of inclusion of information in the final prospectus;
- provide for the treatment of prospectus supplements;
- eliminate the two-year limitation for registered securities for a delayed offering;
- eliminate the at-the-market offering restrictions for issuers registering primary equity offerings on Form S-3 or Form F-3; and
- eliminate the prohibition against immediate takedowns off delayed shelf registration statements.

In addition to the updating of the shelf registration process, the SEC established a significantly more flexible version of shelf registration for offerings by well-known seasoned issuers. This version of shelf registration is called automatic shelf registration.

Under the automatic shelf registration process, eligible well-known seasoned issuers may register unspecified amounts of different specified types of securities on immediately effective Form S-3 or Form F-3 registration statements. Unlike other issuers registering primary offerings on Form S-3 or Form F-3, the automatic shelf registration

process allows eligible issuers to add additional classes of securities and to add eligible majority-owned subsidiaries as additional registrants after an automatic shelf registration statement is effective.

They also can freely accommodate both primary and secondary offerings using automatic shelf registration. Thus, these issuers have significant latitude in determining the types and amounts of their securities or those of their eligible subsidiaries that can be offered without any potential time delay or other obstacles imposed by the registration process. Issuers using an automatic shelf registration statement will be permitted, but not required, to pay filing fees at any time in advance of a takedown or on a pay-as-you-go basis at the time of each takedown off the shelf registration statement in an amount calculated for that takedown.

Rule 415 provides for continuous or delayed offerings and is, therefore, the foundation for shelf registration. Primary offerings on a delayed basis may be registered by certain seasoned issuers only. A number of other delayed or continuous offerings may be undertaken or registered by any issuer, including offerings on a continuous basis of securities issued on exercise of outstanding options or warrants or conversion of other securities, offerings on a continuous basis under dividend reinvestment plans, offerings on a continuous basis under employee benefit plans, and offerings solely on behalf of selling security holders. Rule 415 also permits registration by any issuer of a continuous offering that will commence promptly and may continue for more than 30 days from the date of initial effectiveness.

Many of the types of offerings contemplated by Rule 415 can be accomplished using a prospectus that is complete at the time of effectiveness of the related registration statement and therefore may not require a supplement because there may be no additional information to include in the prospectus. There are a number of offerings contemplated by Rule 415, however, such as a delayed offering, in which the prospectus included in the related registration statement at the time of effectiveness, usually referred to as a base prospectus, must be supplemented to reflect the final terms of the security and offering for each particular offering of securities. In addition, in continuous or delayed offerings employing shelf registration under Rule 415, there may be circumstances where a prospectus will be supplemented other than at the time of a takedown. Rule 424 provides the framework for the filing of each type of prospectus and prospectus supplement.

Filling a regulatory gap, the SEC adopted Rule 430B to specify the relationship between the base prospectus and prospectus supplements and the information that may be omitted from or included in one or the other. This is accomplished by codifying existing practice in most respects and liberalizing the framework for the registration process in certain areas. In addition, Rule 430C was adopted to address the treatment of prospectuses and prospectus supplements for all registered offerings not covered by Rule 430B and for prospectuses not covered by Rule 430A.

Rule 430B is a shelf offering corollary to existing Rule 430A, in that it describes the type of information that primary shelf eligible and automatic shelf issuers may omit from a base prospectus in a Rule 415 offering and include instead in a prospectus supplement, Exchange Act report incorporated by reference, or a post-effective amendment. Rule 430B covers the following types of offerings:

- offerings by well-known seasoned issuers registered on automatic shelf registration statements;
- immediate, delayed, and continuous primary offerings by primary shelf eligible issuers pursuant to Rule 415(a)(1)(x);
- secondary offerings by certain primary shelf eligible issuers, including for the purpose of adding information regarding the identities of and amounts of securities to be sold by selling security holders; and
- offerings of mortgage-backed securities that generally are registered on Form S-11.

Rule 430B provides that a base prospectus that omits information as provided in the rule will be a permitted prospectus. Thus, after a registration statement is filed, offering participants can use a base prospectus that omits information in accordance with the rule. In addition, issuers can communicate using Rule 134 notices, and issuers and other offering participants can use free writing prospectuses under Rules 164 and 433. Rule 430B provides a level of certainty for delayed offerings off of shelf registration statements. Rule 430B also liberalizes current requirements in certain respects, and significantly liberalizes requirements for automatic shelf registration statements.

Rule 430B also establishes a new effective date for a shelf registration statement for Section 11 liability purposes only for the issuer and for a person that is at the time an underwriter. The new effective date will be the date a prospectus supplement filed in connection with the takedown or takedowns is deemed part of the relevant registration statement.

For purposes of liability under Section 11 of the issuer and any underwriter at the time only, the new effective date will be as to the part of the registration statement relating to the securities to which such prospectus relates. The part of the registration statement will consist of all information included in the registration statement and any prospectus relating to the offering of the securities as of the new effective date and all information included in reports and materials incorporated by reference into the registration statement and prospectus as of such date relating to the offering, and in each case, not modified or superseded pursuant to Rule 412.

The part of the registration statement will include information relating to the offering in a prospectus already included in the registration statement. This includes, for example, a form of prospectus containing information relating to the offering and previously filed pursuant to Rule 424(b)(3) other than in connection with the takedown in question, where the information has not been modified or superseded. These provisions also will reconcile the effective date for shelf offerings for issuers and underwriters with a comparable date for non-shelf offerings. The SEC believes that the rule also will eliminate the unwarranted, disparate treatment of underwriters and issuers under Section 11.

Currently, there can be a mismatch between issuers and underwriters in the time that liability is assessed. For example, in an offering off a shelf registration statement, an issuer could have its liability assessed as of the date of the registration statement's initial effectiveness (or post-effective amendment) or the most recent updating required under

Securities Act Section 10(a)(3), while the liability of an underwriter would be assessed at the later time when it became an underwriter.

In such a case, underwriters in takedowns occurring after the date of initial effectiveness (or post-effective amendment) or the Section 10(a)(3) update would be subject to liability under Section 11 for an issuer's Exchange Act reports incorporated by reference into the prospectus included in the registration statement after that date while issuers would not. According to the SEC, Rule 430B results in most cases in the date of effectiveness of a registration statement for an issuer and underwriter in a particular offering being close in time.

For other persons, including directors, signing officers, and experts, the filing of a form of prospectus should not result in a later Section 11 liability date than that which applied prior to the new rules. Thus, generally under Rule 430B, the prospectus filing will not create a new effective date for directors or signing officers of the issuer. Similarly, the SEC did not change the effective date for auditors who provided consent in an existing registration statement for their report on previously issued financial statements or previous reports on management's assessment of internal control over financial reporting, unless a prospectus supplement (and any Exchange Act report incorporated by reference into the prospectus and registration statement) or post-effective amendment contains new audited financial statements or other information as to which the auditor is an expert and for which a new consent is required.

Prospectus Delivery Reforms

The SEC has revised the prospectus delivery requirements in order to facilitate effective access to information, while taking into account advancements in technology and the practicalities of the offering process. These changes are intended to alleviate timing difficulties that may arise under the current securities clearance and settlement system, and also to facilitate the successful delivery of, and payment for, securities in a registered offering. Given that the final prospectus delivery obligations generally affect investors only after they have made their purchase commitments and that investors have access to the final prospectus upon its filing, the SEC believes that the delivery obligation could be accomplished through means other than physical delivery. In addition, because the contract of sale has already occurred, delivery of a written confirmation and the delivery of the final prospectus need not be linked.

The SEC has adopted an access equals delivery model under which issuers, brokers, and dealers can satisfy their final prospectus delivery obligations if a final prospectus is or will be on file with the Commission within the required time, including the cure period. The access concept is premised on the information or filings being readily available. It is also based on the premise that investors have access to the Internet.

Some offerings have been excluded from the access equals delivery model because either they do not raise the same issues, as in corporate capital formation transactions, or they are already subject to rules unique to their offerings. For example, in offerings made

pursuant to Form S-8, the final prospectus is never filed with the SEC and, thus, these offerings do not raise the same types of issues as other capital formation transactions.

Business combination transactions and exchange offers also differ from other types of offerings registered under the Securities Act because the proxy rules and tender offer rules in conjunction with state law impose informational and delivery requirements in those transactions. The information contained in the final prospectus, therefore, will be delivered regardless of the 1933 Act's requirements. Finally, registered investment companies and business development companies will not be able to rely on the rule since they are subject to a separate framework governing communications with investors.

Risk Factor Disclosure

Many Securities Act registration statements require disclosure of the risks associated with an investment in a company's stock. The risk factor section is intended to provide investors with a clear and concise summary of the material risks of such an investment. The SEC has now extended risk factor disclosure to the annual report on Form 10-K. In addition, the Commission requires quarterly updates of risk factors to reflect material changes from previously disclosed risk factors. This disclosure requirement should not be that onerous, according to the SEC, since companies already have in place disclosure controls and internal controls that should alert them to new or changing material risks.

The Commission rejected the suggestion from some accounting firms that risk factor disclosures be extended to small business issuers. Similarly rejected was a suggestion that the risk factor disclosure not be placed in a new Item 1A of Form 10-K. In urging that such disclosure be aligned with the MD&A requirement under Item 7, some commentators reasoned that placing the risk factor disclosure next to the discussion of the business could promote an undesirable tendency to disclose all risks that may affect the entity and its various segments, products, and services discussed in the business section, rather than only the most critical risk factors.

Several accounting firms asked the Commission to provide interpretive guidance regarding the nature and objectives of the risk factor disclosures. According to PricewaterhouseCoopers, this approach will enable a company to customize the discussion to address the relevant risk factors that it believes are necessary for investors and the markets to understand. To facilitate meaningful risk factor disclosures, the Commission should provide guidance similar to that included in several MD&A releases.

Unresolved Staff Comments

The new rules also require accelerated filers and well-known seasoned issuers to disclose, in their annual reports, material and unresolved written comments made by the SEC staff in connection with a review of the company's Exchange Act reports. The disclosure must be sufficient to convey the substance of the comments. Staff comments that have been resolved, including those that the staff and company have agreed will be addressed in future Exchange Act reports, do not need to be disclosed. Further,

companies can provide other information, including their position regarding any such unresolved comments.

A number of accounting firms did not support the proposed disclosure of outstanding comments. They believed that companies already have sufficient incentives to comply with staff comments and that such disclosure may not provide investors with meaningful information. For example, Deloitte & Touche said that the prospect of liability exposure under the antifraud provisions of both the Securities Act and the Exchange Act in connection with material omissions or misstatements provides a significant incentive for companies to address issues identified in staff comments. Ernst & Young asserted that the CEO and CFO certifications required by Sections 302 and 906 of the Sarbanes-Oxley Act already provide added incentive for the timely resolution of SEC staff comments.

But the SEC emphasized that disclosure of outstanding comments is an important component of the securities offerings reforms. Given the fact that enhanced Exchange Act reporting is at the core of the offering reforms, the SEC said it was necessary to establish added incentives for accelerated filers to timely resolve outstanding staff comments on their Exchange Act reports. The Commission rejected a suggestion that companies be permitted to either comply with the disclosure of comments or abstain from conducting an offering until the comments have been resolved.