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New IPO Policy Signals Pragmatic Regulatory Approach

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Law360, New York (July 24, 2017, 1:05 PM EDT) --
A recent policy change at the U.S. Securities and Exchange Commission signals a business-friendly and pragmatic regulatory approach intended to boost the number of initial public offerings.


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Chairman Jay Clayton has made it clear that he is well-aware of the challenges faced by issuers in raising capital in the United States. Recently, the staff of the SEC addressed some of those challenges when it announced a new expanded policy under which it would accept draft registration statements for nonpublic review.

This new policy, which became effective on July 10, 2017, allows all issuers to have their registration statements reviewed on a nonpublic basis for IPOs, U.S. exchange listings such as with spinoffs and direct listings, and follow-on offerings within one year of an IPO or listing.


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The new policy, which was put in place quickly without rule writing or statutory mandate, demonstrates the SEC's willingness to make significant changes in long-standing policy to provide meaningful assistance to issuers seeking to carry out offerings and listings in the United States.

Background


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Companies that raise capital through a public offering of securities are required under the Securities Act of 1933 (Securities Act) to register the offering with the SEC. Registration involves the filing of a registration statement with the SEC containing extensive information about the company's business, financial condition, management and many other matters. The staff of the SEC has the opportunity to review the registration statement and ask the company to revise the financial and other information presented. In response to the SEC's comments, a company will revise its registration statement and the staff will again review the revised information and may ask for further revisions. This back-and-forth process, which can take several weeks, continues until the SEC staff's concerns are satisfied.

In general, all registration statements are required to be filed publicly, as a result of which they are freely available on the SEC's EDGAR website immediately upon filing. Although there is value in the

transparency of the SEC registration process, there are many drawbacks to the public filing of a registration statement for an IPO. Previously undisclosed information, such as revenues, operating margins, senior executive compensation amounts and material contracts, become immediately available to competitors, suppliers and customers long before an issuer can begin to capture the benefits of public company status.

Over time, two exceptions developed to the requirement for public filing of IPO registration statements. First, going back to the early 1990s, the SEC staff permitted non-U.S. companies known as foreign private issuers (FPIs) to submit draft registration statements for review on a confidential basis, with a public filing occurring when the offering was actually ready to launch. Second, in the 2012 Jobs Act, Congress extended confidential submission to all emerging growth companies (EGCs), meaning companies with annual revenues of less than $1.07 billion and meeting certain other requirements. Larger IPO companies that exceeded the revenue threshold or otherwise could not qualify as an EGC, and spinoff companies or others filing initial registration statements under the Securities Exchange Act of 1934 (Exchange Act), were still required to make all their filings public from the start.

New Expanded Policy

In late June 2017, the SEC staff announced that beginning on July 10, 2017, it would expand the circumstances under which it would accept registration statements on a nonpublic basis to include:

- all initial Securities Act registration statements and revisions, regardless of whether the issuer qualifies as an EGC, as long as the issuer agrees to publicly file its registration statement and all nonpublic drafts at least 15 days before the start of any roadshow, or if there is none, before effectiveness;

- all initial registration statements and revisions in connection with a listing on a U.S. stock exchange under Section 12(b) of the Exchange Act, as long as the issuer agrees to publicly file its registration statement and all nonpublic drafts at least 15 days before listing;

- all Securities Act registration statements from any issuer that is submitted no later than the end of the 12th month after the effective date of the issuer's initial Securities Act or Exchange Act Section 12(b) registration statement, as long as the issuer agrees to publicly file its registration statement and the nonpublic drafts at least 48 hours before any requested effective time.

Under this expanded policy, the only initial registration statements that may not be submitted on a nonpublic basis are Exchange Act registration statements under Section 12(g) by U.S. issuers or non-IPO foreign registrants that do not come within the policy for foreign private issuers.

Confidential submissions under the Jobs Act and the new policy must contain all information that a filed registration statement would contain. The new policy provides accommodations relating to the SEC staff's willingness to review registration statements that are not complete to the extent the issuer reasonably believes that omitted financial information will not be required when the registration statement is publicly filed. This relief is similar to that provided under the 2015 FAST Act, which allows an EGC to omit financial information that relates to historical periods that the issuer reasonably believes will not be required at the time of the offering.

In the new policy, the SEC staff also noted its authority to consider requests by issuers to omit or include

alternative financial statements than those that would normally be required under the SEC's rules. Very frequently, companies find that they are required under SEC rules to include audited financial statements relating to companies that they have recently acquired or companies in which they own a significant minority ownership position. This statement, relying on S-X Rule 3-13, signals the staff's willingness to show flexibility in providing relief.

Emerging Questions

The new policy raises a number of implementation questions. The SEC staff has addressed many of these in newly published guidance to assist issuers with some nuances of the new policy. For example, the staff has noted that issuers may use Rule 83 to request confidential treatment for the draft nonpublic submissions under the new policy. Unlike EGC draft submissions, which the Jobs Act expressly exempted from the Freedom of Information Act, nonpublic submissions under the expanded policy remain potentially subject to access under FOIA unless issuers assert Rule 83 protection over the draft submissions.

Other questions that may arise could relate to how the SEC staff will treat acceleration requests in the context of the 48-hour public filing requirement for follow-on offerings. An acceleration request ordinarily must occur at least two business days before effectiveness unless waived by the staff, whereas 48 hours can elapse over a weekend between a Friday afternoon filing and a Monday morning launch. We expect that the staff will consider these scenarios on a case-by-case basis and will strive to be accommodating toward reasonable requests.

Other implementation questions remain at this early stage. For example, it is currently unclear whether a company that has submitted a confidential draft registration statement for a follow-on primary equity offering that did not go forward and was never publicly filed may seek to submit a new confidential draft registration statement for a different offering, such as a follow-on secondary offering of equity securities or a primary offering of debt securities. Also, it is currently uncertain whether the staff will require underwriters to be named in any follow-on confidential submission relating to a firm-commitment offering or whether the staff would be willing to provide first-round comments prior to the issuer naming underwriters.

Traps for the unwary may arise because EGCs are permitted to discuss a planned offering with certain institutional investors prior to the public filing of a registration statement under the so-called "testing the waters" (TTW) provision of the Jobs Act. Companies that are not EGCs do not have similarly broad latitude, and counsel must be careful to distinguish between situations involving draft submissions made by EGCs, which can engage in TTW communications, versus those made by non-EGCs, which cannot.

Looking Ahead

We welcome the new policy, and hope that it is a leading indicator of further innovative action by the SEC and its staff to spur capital formation through IPOs and other registered offerings.

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