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Client Alert

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The Bought Deal Bible: A User's Guide to Bought Deals and Block Trades

"This *Client Alert* provides a comprehensive review of all of the legal and practical issues you will face in executing a bought deal. In Annex A, we have included a sample timeline for a registered bought deal that will help you get control of the process."

It's Monday morning and you've been told that your favorite seasoned issuer is planning a bought deal that is scheduled to launch after the close of trading on Wednesday. What do you do? Well, you don't need to panic — we have you covered. All you need to do is answer the following simple questions:

- Will it be a public offering?
- Is the issuer a well-known seasoned issuer?
- Is there available room under an effective shelf?
- Does the issuer's disclosure need topping up in light of recent or pending events or announcements?
- Does the issuer need to file a Form 8-K with any necessary topping up disclosure or will a prospectus supplement or press release be sufficient?
- Is the fact that a deal is pending material?
- Will the underwriter be pre-marketing the deal prior to public announcement?
- Will the underwriter be wall-crossing potential investors prior to announcement?
- Will the underwriter need to promise wall-crossed accounts a "free-to-trade" date that might require issuer disclosure if the deal does not proceed?
- Will the underwriter need a preliminary prospectus supplement at the time of launch?
- Will there also be a press release at the time of launch?
- Will the sale by the underwriter be in a fixed price offering or a variable price reoffering?
- Will there be a "pricing" press release after pricing?
- Will there be any selling stockholders?
- Do the selling stockholders (or their board designees) have any material non-public information?
- Are there any underwriting agreement issues to be negotiated?
- What lock-ups will be required from existing stockholders, if any?
- Are there any NYSE or Nasdaq issues to consider?
- Will a FINRA filing be required?
- Are there any "blue sky" issues?
- Are there any difficult comfort or due diligence issues?

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This *Client Alert* provides a comprehensive review of all of the legal and practical issues you will face in executing a bought deal. In Annex A, we have included a sample timeline for a registered bought deal that will help you get control of the process. You now have the tools you need to answer all of these questions.

For simplicity's sake, we will start by discussing bought deals as if they are always for the account of the issuer. In practice, however, this is often not the case. There are a number of special issues that apply to bought deals involving resales of outstanding securities by selling stockholders. We review those issues below under "Special Issues in Secondary Trades."

What's a Bought Deal or a Block Trade Anyway?

In this *Client Alert*, when we refer to a "bought deal," we mean a securities offering in which an underwriter agrees to purchase an issuer's securities at an agreed price (or pricing formula) without a prior marketing process. The term "block trade" means a sale of a block of securities (typically 10,000 or more shares of stock or $200,000 or more in principal amount of bonds) and is often used interchangeably with the term bought deal, particularly where the seller is an existing stockholder rather than the issuer.

A bought deal decreases execution risk for the issuer or selling stockholder and shifts market risk to the underwriter earlier in the transaction by allowing sellers of securities to lock in the seller's price before launch and without an extensive issuer marketing process. Of course, there is no such thing as a free lunch. Bought deals demand execution within a very quick timeframe, while at the same time requiring the maintenance of customarily strict due diligence and documentation standards. They are not for the faint of heart.

SIFMA Guidelines

In March 2008, the Securities Industry and Financial Markets Association published a set of guidelines for bought deals entitled "Block Trade Guidelines."[1] The SIFMA guidelines emphasize the importance of having all documentation ready prior to launch to enable the underwriter to confirm trades as soon as a deal is struck between the issuer and the underwriter.

Preparedness is everything in the context of a bought deal. Delay can result in major financial losses — minutes can mean millions of dollars.

Shelf Registration

The first question to ask when contemplating a registered bought deal is whether the issuer has an effective shelf registration statement with sufficient available capacity. If so, you're off to the races.[2]

Even if not, you're still good to go if the issuer qualifies as a well-known seasoned issuer, since WKSIs can file an immediately effective automatic shelf registration statement on Form S-3 without SEC Staff review.[3] Non-WKSI issuers without an effective shelf registration statement, by contrast, will not be in a position to consider a registered bought deal, because they will not typically have the time to wait for a new Form S-3 to become effective. As a result, bought deals for non-WKSI issuers are sometimes accomplished through an exempt offering. Bought deals involving newly issued common stock are usually done on a registered basis, however, because the Rule 144A exemption from registration is generally not available for securities that are fungible with a class of securities listed on a US national securities exchange, *e.g.*, common stock listed on the NYSE or the Nasdaq.

If the issuer has an effective shelf, the question becomes whether there is sufficient capacity under the shelf to do the bought deal. Once again, it's good

to be a WKSI. In the first place, a WKSI shelf can be filed without specifying a deal size or a number of securities under Securities Act Rule 430B(a). Instead, a WKSI can rely on the "pay-as-you-go" provisions of Securities Act Rules 456(b) and 457(r) to pay fees at the time the final pro supp for the offering is filed under Rule 424(b). Even if the WKSI shelf specifies a maximum deal size and there is insufficient remaining capacity, a WKSI can simply file a new, immediately effective automatic shelf.

Issuers that are Form S-3 eligible but are not WKSIs don't enjoy the luxuries of an automatically effective registration statement or the pay-as-you-go fee system. Their options are much more limited if they have insufficient shelf capacity remaining for the proposed bought deal. One possibility is to upsize an existing shelf by filing an immediately effective short-form registration statement under Securities Act Rule 462(b). However, the Rule 462(b) option can only be used once per shelf and is limited to 20 percent of the remaining unused capacity of the original shelf.[4] The issuer could, of course, file a new Form S-3 registration statement, but that would introduce timing uncertainties. Even if the SEC Staff chooses not to review the new registration statement, that determination itself takes a few days, and the shelf filing may send signals to the market and generate downward selling pressure that the issuer would prefer to avoid. Given these limitations, a non-WKSI issuer should file a shelf registration statement well in advance of an anticipated bought deal and pay the requisite filing fees for any and all securities anticipated to be sold in the offering.[5]

When considering whether a currently effective Form S-3 shelf is suitable for a planned bought deal, keep in mind that a shelf for a primary offering (WKSI or non-WKSI) has a three-year life after its initial effective date by virtue of Securities Act Rule 415(a)(5). Obviously, this time limit poses a less significant obstacle for WKSIs than for non-WKSIs, given that a WKSI can simply put up a new automatic shelf registration statement. You should be aware of the possibility that a particular bought deal may not be successfully resold immediately, in which case an expiring underlying shelf can be problematic. Note also that the expiration date issue does not apply to resale shelf registration statements covering resales by selling stockholders.

Assessing Your Disclosure Package: The Section 11 and Section 12 Files

The Section 11 File

Section 11(a) of the Securities Act imposes liability if any part of a registration statement, at effectiveness, contained a material misstatement or omission. Section 11 liability covers only the registration statement and information included in the registration statement (and accordingly, would not typically cover free writing prospectuses or road show slides).

For the purposes of this *Client Alert*, we use the term "Section 11 file" to cover all of the information deemed to be part of the registration statement at the relevant moment of effectiveness.

A shelf registration statement can have multiple effective times:

- the time of original effectiveness;
- the time a post-effective amendment became effective;
- the time of filing an annual report that is incorporated by reference in the shelf and acts as an update under Securities Act Section 10(a)(3); and
- at each takedown off the shelf.[6]

As a result, the Section 11 file changes over time. In a bought deal, the original effective date of a shelf registration statement is usually the least interesting moment because subsequent Exchange Act reports and pro supp filings will, over time, supersede or modify the

information in the shelf registration statement's base prospectus. The deal team will instead want to focus on whether the Section 11 file is accurate and complete at the time of launch.

If the deal team determines that the Section 11 file needs to be updated before launch, one option is to add any missing information by means of a final pro supp filed under Rule 424(b). That pro supp is typically filed at the very end of the second business day after pricing, and the information it contains is retroactively deemed part of the Section 11 file at the time of the first contract of sale by virtue of the magic of Rule 430B(f). The other way to "top up" the Section 11 file is to make a pre-launch Exchange Act filing (such as a press release filed on Form 8-K) that will be incorporated by reference into the shelf registration statement.

The Section 12 File

By contrast to Section 11, Section 12 of the Securities Act imposes liability on any person who offers or sells a security in a registered offering by means of a prospectus, or any oral communication, which contains a material misstatement or omission. Section 12 looks to the sum of what investors have been told up to the time the underwriter confirms orders. In the context of a bought deal, Section 12's focus is the base prospectus (together with any incorporated Exchange Act filings), any preliminary pro supp sent to investors and any additional information that may have been conveyed to investors (orally or in writing) on or before the time orders are confirmed. For the purposes of this *Client Alert*, we refer to this collection of information as the "Section 12 file."

To determine what additional information needs to be communicated to investors in connection with a bought deal, the issuer will need to focus on the adequacy of each of the Section 11 file and the Section 12 file at launch. If an important event in the issuer's business has occurred or is pending, or if the issuer expects to announce earnings shortly after the offering, the deal team will want to consider whether additional disclosure is required before launch. For just this reason, many bought deals are timed to follow promptly after an earnings release or the filing of a periodic report.

Regulation FD

Regulation FD requires an issuer to publicly disclose any material, non-public information simultaneously with its intentional disclosure to members of the financial community. The plan to launch a bought deal can itself be a material fact in some cases. To comply with Regulation FD, the issuer will need to publicly announce the launch of any bought deal that is material to the issuer prior to approaching potential investors.

Determining whether the coming launch of a particular bought deal is material to the issuer will always depend on all of the facts and circumstances. Consider the following presumptions as helpful rules of thumb:

- an issuance of common equity, convertible notes or high yield bonds is presumptively material;
- an issuance of investment grade bonds is presumptively not material; and
- a resale of outstanding shares of common stock by an existing stockholder is sometimes material and sometimes not material.

Like all rules of thumb, these three are only the starting point in an analysis that must take into account all relevant facts and circumstances, including disclosures in previously filed Exchange Act documents about the issuer's financing plans and the importance of a particular transaction to the issuer's business.

Testing the Waters

Regardless of whether a particular bought deal is initiated by the underwriter or the issuer, the underwriter may want to engage in a

limited pre-marketing process before submitting its bid to the issuer. This is only natural, since the underwriter will want to avoid a scenario in which it is unable to sell the "bought" securities at or above the agreed-upon price paid to the issuer. When pre-marketing a bought deal to potential investors, the underwriter will need to be cognizant of both the SEC's restrictions on offers and Regulation FD's prohibition on selective disclosure. The issuer will want to review and discuss the underwriter's pre-marketing plans in order to satisfy itself that Regulation FD will be complied with and that the underwriter is communicating appropriately with potential buyers. Many issuers like to keep tight control over these pre-marketing efforts to avoid the risk of market movement prior to the official launch of the deal.

The Restrictions on Offers

If an underwriter inquires of individual investors as to their appetite for a particular security of a particular issuer, the question arises as to whether that inquiry amounts to an "offer" of the security being discussed.[7] Oral offers to sell securities are permissible if the securities are covered by a previously filed registration statement. If a registration statement has not already been filed, then all offers are prohibited unless the issuer is a WKSI offering its own securities directly to investors or the offering is exempt from registration under Rule 144A, Regulation S or another exemption.

Securities Act Rule 163 allows WKSIs to make unrestricted oral and written offers of their own securities prior to the filing of a registration statement. However, this WKSI exception applies only to offers made by the WKSI itself, and does not allow the underwriter to make pre-filing offers on a WKSI's behalf.[8] As a result of the limitations of Rule 163, an underwriter is able to make pre-marketing offers in registered offerings only after the issuer has filed a registration statement. WKSIs can enable an underwriter to make such offers simply by filing an automatic shelf, but some WKSIs are hesitant to do so because a shelf filing will signal to the market the likelihood of an offering and thereby create execution and market risk and, possibly, downward pressure on its stock price.

Wall-Crossing and Testing the Waters

An underwriter desiring to determine market demand for securities that may shortly be offered in a bought deal also needs to be concerned about Regulation FD if the fact that the issuer is planning an offering is itself material non-public information. There are at least two ways that the underwriter might "test the waters" with the particular accounts it expects to participate in an offering. Each of these techniques has different consequences under Regulation FD.

If the underwriter wants to gauge investor interest *without* restricting the investors with whom it speaks, the underwriter may make "no names" inquiries about investor appetite for specific securities of a broad range of issuers in a particular industry sector. In that case, especially if the underwriter has not yet been approached by the issuer about a possible offering, the underwriter may be able to conclude there is no Regulation FD or selective disclosure issue and, hence, no need to restrict the investors with whom it speaks.

In order to test the waters about a particular bought deal that is material to the issuer prior to the public announcement of the deal, the underwriter may want to "name names" and get a more concrete estimate of investor interest. To do that, the underwriter will ask the potential investor if it is willing to be "wall-crossed" (*i.e.*, moved to the restricted side of the firm's trading wall) as to an unnamed issuer in a particular industry.

If the investor agrees to be restricted, the underwriter may send the investor an email confirming its willingness to keep confidential whatever it is about

to learn, although some underwriters take the view that the investor's verbal acknowledgement of the confidentiality arrangement is sufficient to establish the existence of an express agreement for Regulation FD purposes.[9] Some underwriters also ask for a return email from the investor acknowledging the confidentiality arrangement.

Prior to agreeing to be wall-crossed, most investors will want to agree on a future date (often not more than a few days out) when the wall-cross trading restrictions will lapse. The issuer will ordinarily participate in determining the free-to-trade date, since the issuer may have a part to play in publicly disseminating the information necessary to ensure free tradability by a date certain.

Once the investor has agreed to be wall-crossed, the underwriter can name the issuer and have an explicit discussion with the investor about its interest in participating in the upcoming offering, subject only to the restrictions on offers described above.

Launching the Deal and Post-Launch Communications

The underwriter will want to publicly announce the deal and begin allocating securities to buy-side accounts as soon as the issuer accepts its bid. The public announcement of launch serves as a "for sale" sign to the market and satisfies any Regulation FD concerns about selective disclosure. In most cases, the issuer and the underwriter will agree on a price immediately after the close of trading (4:00 p.m., New York City time). The underwriter will expect to begin reselling the bought securities immediately and will hope to have the entire deal sold prior to the open of trading on the next day (9:30 a.m., New York City time). Because this time period is critical to the underwriter's marketing efforts, it is essential that all documents be finalized ahead of time so that the deal can be publicly announced as soon as the issuer accepts the underwriter's bid.

The form of the announcement that is appropriate for a given bought deal depends upon the adequacy of issuer information already available to investors by way of prior Exchange Act filings, the nature of the security being offered and the proposed manner of resale by the underwriter.

Getting the Word Out

There are a number of ways to announce a bought deal, including a Rule 134-compliant press release filed or furnished on Form 8-K, a preliminary pro supp filed under Rule 424(b) or, preferably, both.[10] A bought deal can also be launched using an issuer FWP under Rule 433. Whichever approach is chosen, the issuer must carefully consider whether the announcement, when taken together with all other information made available to investors in the registration statement and incorporated Exchange Act filings, conveys all the information required to be disclosed under the federal securities laws.

- *Rule 134 Press Release.* Rule 134 enables an issuer with an effective registration statement to issue a press release that includes certain limited information related to an offering without the communication being deemed to be a prospectus or an issuer FWP.[11] The use of a Rule 134-compliant press release is the most common way to announce the launch of a bought deal because it can be prepared and disseminated quickly. A press release has the added benefit of satisfying the requirements of Regulation FD, particularly if it is concurrently filed on Form 8-K.[12] Although a press release is an effective way to announce a bought deal, the issuance of the release alone will not serve to update the Section 11 file — it will need to be filed on Form 8-K to achieve that goal. The SIFMA Block Trade Guidelines include a recommended form of launch press release for both primary and secondary sales of common stock.

- *Preliminary Pro Supp.* For an issuer desiring to top up the Section 12 file at the moment of launch, a preliminary pro supp is a good way to go. The use of a preliminary pro supp filed under Rule 424(b) immediately prior to the launch of the offering provides the underwriter with a comprehensive method of announcing the offering and the terms of the securities as well as any other information the deal team determines is appropriate to add to the Section 12 file. A publicly filed preliminary pro supp also constitutes public disclosure of the deal that satisfies Regulation FD (although many issuers choose to issue a press release and file it on Form 8-K concurrently with the Rule 424(b) filing immediately prior to launch). For these reasons, some underwriters opt to use a preliminary pro supp in every deal, whether it is strictly necessary or not. On the other hand, some underwriters will agree to dispense with a preliminary pro supp where there is no need to convey additional information to accounts prior to confirming orders.

Post-Launch Communication

The customary practice for issuer communications after a bought deal has been launched is directly related to the manner of distribution by the participating underwriter. Let's review the two methods of resale used by underwriters to distribute a bought deal.

Fixed Price Offering

In a fixed price offering, the underwriter purchases the shares from the issuer or the selling stockholders and reoffers the shares to the public at a fixed price, often called the "clearing price." In these transactions, the underwriter expects to sell all of the shares on offer at the clearing price, although the plan of distribution language in the base prospectus normally includes language allowing the underwriter to change the pricing at any time without notice (in case it turns out to be a "sticky" deal).

Variable Price Reoffering

In a variable price reoffering, the underwriter resells the purchased securities at variable prices as determined by market conditions and subsequent negotiations with buy-side accounts.

Since the issuer cannot know at the time its shelf registration statement is initially filed with the SEC what method(s) of distribution will be used by its underwriters in future takedowns, the issuer should include broad language in the base prospectus so there will be no need for an update at the time of a takedown. We suggest including language in the plan of distribution section of the base prospectus to the effect that:

> "We may sell the securities covered by this prospectus in any of three ways (or in any combination): (i) to or through underwriters or dealers; (ii) directly to one or more purchasers; or (iii) through agents.
>
> We may distribute the securities covered by this prospectus from time to time in one or more transactions: (i) at a fixed price or prices, which may be changed from time to time; (ii) at market prices prevailing at the time of sale; (iii) at prices related to the prevailing market prices; or (iv) at negotiated prices.
>
> Each time we offer and sell securities covered by this prospectus, we will make available a prospectus supplement or supplements that will describe the method of distribution and set forth the terms of the offering, including: (i) the name or names of any underwriters, dealers or agents and the amounts of securities underwritten or purchased by each of them; (ii) if a fixed price offering, the public offering price of the securities and the proceeds to us; (iii) any options under which underwriters may purchase additional securities from us; (iv) any underwriting discounts or commissions or agency fees and other

items constituting underwriters' or agents' compensation; (v) terms and conditions of the offering; (vi) any discounts, commissions or concessions allowed or reallowed or paid to dealers; and (vii) any securities exchange or market on which the securities may be listed."

However, even if the issuer omits this broad description of offering methods in the plan of distribution section of the base prospectus, a WKSI can add this disclosure by means of a pro supp under Rule 430B(a).[13]

There are generally two types of post-launch communications associated with bought deals: (i) a "pricing" press release issued as soon as the clearing price in a fixed price offering has been established and (ii) the required final pro supp filed pursuant to Rule 424(b).

The Pricing Press Release

There is no specific SEC rule requiring the issuer to publicly announce the results of its offering prior to filing the final pro supp pursuant to Rule 424(b) (which can be as late as 5:30 p.m. on the second business day after pricing). However, if the offering is a primary offering, the issuer will have two reasons to consider issuing a pricing press release once the deal has been sold and the clearing price has been established.

First, there may be a Regulation FD concern in some cases if the clearing price is known to some market participants and not others. A pricing press release that discloses the clearing price and is filed on Form 8-K completely eliminates any Regulation FD concern.

Second, the NYSE takes the position that a pricing press release is necessary if either the underwriting discount or the clearing price is itself material information.[14] If the NYSE determines that these pricing terms are material, it may refuse to open the issuer's stock for trading following an overnight bought deal until a pricing press release has been issued. Obviously, no one wants to see that happen. For this reason, even where the deal team determines that neither the clearing price nor the underwriting discount is material, it is prudent to have a pricing press release drafted and ready to go in case the NYSE sees it differently. In fact, some underwriters advise their clients to issue a pricing press release in every fixed price deal as a preemptive measure.

In practice, the NYSE will often seek the views of the issuer and its counsel on the question of whether the underwriting discount or the clearing price for a particular bought deal is material. Materiality in this context, as always, depends on all of the facts and circumstances. The NYSE does not apply any bright-line tests, but our experience suggests that, if the underwriter purchases shares for less than 85-90 percent of the last closing price, you should expect to have a conversation with the NYSE about disclosure before the start of trading.[15] Even where the underwriter's purchase price is more than 90 percent of the last closing price, the NYSE may want to have a discussion with the issuer or the underwriter about the size of the underwriting discount or the clearing price before acquiescing to the materiality judgment of the deal team, which can have the effect of slowing down the transaction and possibly even delaying the opening of the stock. Remember that the NYSE expects a phone call at least 10 minutes before any material news is released during the trading day or shortly prior to open so it can make a determination of whether to halt trading while the market absorbs the new information. Nasdaq does not currently expect its listed companies to issue a press release following the pricing of a bought deal.

Filing the Final Pro Supp

The final pro supp is a particularly interesting document in a bought deal. The pricing information that first appears in the final pro supp is the focus of extra attention in the bought deal world. The price per share paid by the

underwriter in a bought deal is typically determined based on a discount to the closing price per share of the issuer's stock on the day prior to launch. In some cases, the agreed-upon price is based on a formula that takes into account the clearing price, once known. Underwriters generally prefer to utilize the entire two business day-period contemplated by Rule 424(b) before filing the final pro supp.

Disclosing the pricing information, including the underwriter's discount, in the final pro supp has the effect of including the information in the Section 11 file (by virtue of the magic of Rule 430B), but it does nothing for the Section 12 file. Most issuers and underwriters conclude that an underwriting discount that is within a customary range is not material and, therefore, need not be included in the Section 12 file (*i.e.*, can be omitted from the launch press release and the preliminary pro supp). However, each deal team should consider the facts and circumstances surrounding its particular offering before determining that omitting the underwriter's discount (and hence the net proceeds to the issuer) from the Section 12 file at the time of sale is acceptable. Some of the factors a deal team may wish to consider in this regard include the size of the discount as compared to the closing price of the security on the day prior to launch, whether the bought deal is a primary or secondary offering, the intended use of proceeds from the offering and whether the security in question has a high trading volume. Hard and fast rules are rarely useful in the context of an offering, but it's worth noting that public disclosure of underwriter discounts and issuer net proceeds prior to the filing of the final pro supp is quite rare in the context of bought deals.

Special Issues in Secondary Trades

Sales of securities in bought deals by existing securityholders typically involve sales of common stock by affiliates of the issuer. Non-affiliates holding restricted common stock can usually resell under Rule 144 without much (or any) underwriter assistance, but affiliates who want to reduce or exit their investment in a particular issuer are subject to Rule 144's rather significant volume limitations.

A number of important issues arise in the context of resale bought deals that do not exist in bought deals for the account of the issuer. Let's examine the three most important issues.

Special Due Diligence Concerns

Sections 11 and 12 of the Securities Act provide underwriters with a due diligence defense to liability. Therefore, the underwriter in a bought deal will want to conduct a reasonable investigation to get comfortable that the issuer's disclosures (including, if applicable, the disclosure in the preliminary pro supp) are accurate and complete in all material respects. The added challenge in the context of a secondary trade is that the selling stockholder will likely not have unlimited attention from the issuer's management. Even though registered resale transactions almost always involve resales by controlling affiliates of the issuer, "control" for purposes of determining affiliate status is not always the same as control for purposes of a due diligence effort. The deal team will need to construct a reasonable investigation that suits the circumstances of the particular transaction. One size does not fit all.

The "Clean Hands" Representation

Whenever an affiliate is selling securities, the question arises whether the affiliate has had access to material information that is not in the public domain — for example, knowledge of early-stage acquisition or divestiture discussions. In most circumstances, the selling affiliate provides the underwriter with a "clean hands" representation to the effect that the affiliate is not in possession of (or making its "sell"

decision on the basis of) any material non-public information. If the selling affiliate is in possession of material non-public information, it is always possible to level the playing field by disclosing that information to the public in a preliminary pro supp prepared specifically for the offering or by filing a Form 8-K prior to launch, but the issuer may not be prepared to make public disclosures about future plans that are not yet finalized. Many issuers are reluctant to make special out-of-cycle disclosures to facilitate resales by affiliates. And most issuers have insider trading policies that limit affiliate resales to trading windows following Exchange Act filings. In many cases, the right decision is for the affiliate to keep out of the market until a pending transaction has been publicly announced or formally abandoned.

These selective disclosure concerns are often addressed by timing a resale bought deal to follow promptly on the heels of the filing of a periodic report by the issuer. The various disclosure requirements applicable to Exchange Act reports, particularly annual reports on Form 10-K and quarterly reports on Form 10-Q, are sufficiently comprehensive that the deal team can usually conclude that the public disclosure file is complete following a periodic report filing. The same conclusion may be possible following the filing of an earnings release in some cases. Note, however, that an earnings release that is merely "furnished" on Form 8-K will not be considered to be part of the Section 11 file, which may indicate the need for a final pro supp that includes a "recent developments" section.[16]

Special FINRA Issues

Bought deals involving securities of seasoned issuers do not, as a general rule, require a filing with, or review by, FINRA, as we will discuss in greater detail below. However, FINRA uses a different standard from that used by the SEC for determining "seasoned" status. As a result, not all WKSIs are seasoned issuers in FINRA's world. FINRA will expedite the review of a primary offering for an unseasoned WKSI or non-WKSI issuer under certain circumstances, but it will not currently promise expedited or same-day clearance for a secondary offering of securities of an unseasoned WKSI or non-WKSI issuer. If this is your scenario, early communication and coordination with FINRA may become central to your deal timing.

Exempt Bought Deals

So far in this *Client Alert*, we have discussed bought deals in the context of a registered offering only.[17] However, executing a bought deal on an exempt basis is a viable option for US issuers offering straight debt or convertible securities when an effective registration statement is not available.[18] The private market for debt and convertible debt securities of issuers that are seasoned enough to be considering a bought deal is deep and wide. Limiting the universe of available purchasers to qualified institutional buyers and non-US investors doesn't typically affect the execution of such an offering, or the price at which underwriters are willing to purchase the securities, because institutional investors are the accounts targeted in offerings of straight debt and convertible debt securities. Of course, privately placed securities are "restricted securities" subject to Rule 144's restrictions on trading, which may necessitate a modest liquidity discount.

There are a few additional benefits of an exempt bought deal worth noting.

Disclosure and Other Regulatory Obligations

Exempt offerings generally are not subject to FINRA's corporate finance filing requirement and related review process, which can require significant lead time.[19] The underwriter also has additional flexibility to pre-market an exempt offering as compared to a registered offering because none of the restrictions on offers under Section 5 of

the Securities Act apply in the context of an exempt offering, other than the prohibition on general solicitation. The underwriter may also prefer an exempt offering because Sections 11 and 12 of the Securities Act do not apply to unregistered transactions.[20] In addition, there may also be deal-specific issues that prevent an issuer from consummating a registered offering that can be avoided through an exempt offering. For example, if an issuer does not have the necessary financial information available to satisfy all of the applicable requirements of Regulation S-X, the issuer and the deal team may be able to conclude that satisfaction of some of the more technical Regulation S-X requirements is not required by sophisticated institutional investors. In those cases, a private offering may be a viable option even if a registered offering is not.

Regulation M

Regulation M is designed to prohibit manipulation of the price of a security (or certain related securities) during a "distribution" of the security. Rule 101 of Regulation M covers distribution participants (including any underwriter, prospective underwriter, broker, dealer or any other person who has agreed to participate or is participating in a distribution), while Rule 102 covers the issuer and any selling securityholder.

Regulation M broadly prohibits covered persons from directly or indirectly bidding for, purchasing, or inducing others to bid for or purchase, covered securities until a specified restricted period for the distribution has ended. Although Rule 101 of Regulation M includes an exemption for trading by distribution participants during a distribution by an issuer with "actively traded securities,"[21] no such exemption exists under Rule 102 for the issuer itself or for a selling securityholder. However, there is a broad exception from the restrictions of Regulation M for a "pure" Rule 144A exempt offering (meaning an offering and sale in the United States only to qualified institution buyers). Accordingly, in a Rule 144A exempt offering, distribution participants, issuers and selling stockholders can bid for or purchase the securities being distributed, even during the offering.

Lock-Up and Clear Market Considerations

To facilitate a successful distribution of the securities the underwriter commits to purchase in a bought deal, the underwriter will typically require that the issuer, certain company insiders and any selling stockholders contractually agree not to sell any of the covered securities into the market for a period of time after the offering. To the extent that the applicable sellers are party to the underwriting agreement, this covenant can be included in the underwriting agreement itself. Otherwise, the restrictions are set forth in a separate lock-up agreement. If your deal has a lock-up provision (in either the underwriting agreement or in a separate lock-up agreement), consider whether the terms of the lock-up, including any negotiated carveouts, should make their way into the Section 12 file. If so, a preliminary pro supp or an issuer FWP may be necessary.[22]

While the lock-up period is often a heavily negotiated offering-specific term, in the context of a bought deal, the restricted period typically ranges from 30 to 90 days. Bear in mind that many bought deals are timed to follow promptly on the heels of an earnings release or the filing of a quarterly or annual report to coincide with a trading window in the issuer's insider trading policy (in the case of a secondary trade) and to avoid the need for topping-up disclosure prior to launch. Accordingly, selling stockholders may look to negotiate a lock-up period that ends prior to the anticipated date of the next quarterly earnings release, which will likely be their next opportunity to access the market.

Even if the negotiated lock-up period expires before the next earnings release, the deal team will need to take into account the prohibitions of FINRA's equity research rule, NASD Rule 2711. Absent an exemption, Rule 2711 prohibits a FINRA member that acted as a manager or co-manager of a public offering from publishing a research report on, or making a public appearance regarding, the applicable issuer during the 15 days prior to and after the expiration, waiver or termination of a lock-up agreement. To the extent that a lock-up expires or is waived in close proximity to the end of an issuer's fiscal period, Rule 2711 can prove problematic because research analysts often publish reports on or make appearances regarding an issuer shortly following an issuer's earnings announcement. In order to protect the research analysts' ability to publish reports or make appearances following an earnings release or similar event affecting an issuer, lock-up agreements typically include a "booster shot" provision that automatically extends the term of the lock-up for up to an additional 34 days if the expiration or termination of the lock-up would otherwise trigger Rule 2711's research quiet provisions.

However, the booster shot can also serve as an impediment to an issuer or selling stockholder looking to launch a bought deal shortly after the publication of the next earnings release. Fortunately, Rule 2711 provides FINRA members some relief from the restrictions to the extent the company in question is (i) an issuer with "actively traded securities" as defined in Regulation M *and* (ii) the member seeking to publish or make a public appearance could issue research reports in accordance with the requirements of Securities Act Rule 139. If these conditions are met, the FINRA member may make a public appearance or issue a Rule 139-compliant research report during the 15-day period prior to, and during the 15-day period following, an earnings release or other issuer announcement — activities that would otherwise be prohibited under Rule 2711.[23] Accordingly, sellers may choose to structure the lock-up agreement such that the related booster falls away to the extent that the issuer qualifies for Rule 2711's actively traded security exemption and the underwriter can issue Rule 139-compliant research on the issuer at the time the lock-up would otherwise expire.

Other Required Filings

To avoid speed bumps, the deal team should plan ahead with respect to all aspects of the required documentation, including any required FINRA, stock exchange or state blue sky law filings.

FINRA Filings

FINRA reviews, among other things, the underwriting and other terms and arrangements relating to the distribution of securities by its members (*e.g.*, a US underwriter in a bought deal) to ensure that such terms and arrangements are not "unfair or unreasonable." Pursuant to FINRA Rule 5110 (also known as the "Corporate Financing Rule"), all US public debt and equity offerings must be filed with FINRA for review and approval prior to making any sales, unless an express exemption is available.

The Seasoned Issuer Exemption

There are several filing exemptions under Rule 5110,[24] however, in the context of a bought deal the most relevant exemption is commonly referred to as the "seasoned issuer exemption."

The seasoned issuer exemption is available for offerings "registered with the SEC on registration statement Forms S-3 or F-3 pursuant to the standards for those Forms prior to October 21, 1992 and offered pursuant to Rule 415 of SEC Regulation C."[25] The pre-October 1992 Form S-3 eligibility criteria required an issuer to have at least 36 months of Exchange Act reporting history and either a $150 million public float or at

least a $100 million public float coupled with an annual trading volume of at least three million shares. Note the importance of this exemption in the context of a bought deal — no FINRA filing will be required if the issuer met the pre-October 1992 Form S-3 eligibility criteria at the time the shelf was filed and continues to meet such criteria at the time of the shelf takedown for the bought deal.

If this is not the case, however, the deal team will need to review the particular facts and circumstances to determine whether a filing is needed for the takedown. For example, a FINRA filing could be required if the issuer met the pre-October 1992 Form S-3 eligibility citeria at the time of the original shelf filing but no longer meets such criteria at the time of the takedown. A filing could also be required if the issuer meets the pre-October 1992 Form S-3 eligibility criteria at the time of the takedown but did not meet such criteria at the time the shelf was filed.[26]

Unfortunately, the definition of a WKSI in Rule 405 does not track the pre-October 1992 Form S-3 eligibility criteria, in particular with respect to the three-year Exchange Act reporting history. As a result, even though a WKSI can file an automatically effective shelf registration statement, a FINRA filing may nonetheless be required in connection with an underwritten offering of a WKSI's securities. The FINRA staff, however, has indicated that they will expedite the review and approval process for WKSIs that are not yet considered seasoned issuers and will endeavor to complete the review process within 24 hours (and typically will complete the process in a much shorter period if alerted in advance and if there are no difficult compensation issues that require a more extensive discussion with senior staff). Nonetheless, failure to recognize early in the process the requirement to effect a FINRA filing in connection with a bought deal can cause additional delay. Accordingly, before finalizing the timeline for a proposed bought deal, the deal team should first assess whether the seasoned issuer, or any other exemption, applies to the offering.

In addition, the seasoned issuer exemption does not necessarily apply to offerings that fall within the "conflict of interest" provisions of FINRA Rule 5121. Even if the issuer would otherwise be exempted from a FINRA filing, the presence of a conflict of interest may trigger the need for a FINRA filing. The most common situations that give rise to a conflict of interest are an underwriter being deemed to be under common control with an issuer or where more than 5 percent of the net proceeds from the offering will be used to repay certain indebtedness owed to the underwriter or its affiliates or is otherwise intended to be directed to the underwriter or its affiliates.[27]

Conflicts of interest must always be disclosed in the offering materials and, under certain circumstances, a qualified independent underwriter, or "QIU," must be engaged to participate in the preparation of the registration statement and the prospectus or other offering document and exercise the usual standards of due diligence in connection therewith. If QIU participation is required, the seasoned issuer and other filing exemptions will not be available and FINRA approval must be obtained prior to making any sales of the offered securities. Given the tight timing of bought deals, an analysis of potential conflicts of interest (including those arising as a result of concurrent or pending transactions) should be performed at the outset and taken into consideration when selecting underwriters.

Preparing for FINRA in Advance

If a determination has been made that a FINRA filing will be necessary, there are a few steps that an issuer can take in advance to help facilitate a smooth FINRA process on the day the bought deal is launched.

Although the underwriter of a future bought deal will almost certainly not have been identified at the time the shelf registration statement of a non-WKSI is first filed with the SEC, FINRA will accept a filing by issuer's (or designated underwriter's) counsel that requests conditional clearance on the base prospectus concurrently with or following the time the shelf registration statement is filed with the SEC. Another filing is required when the underwriter for a particular bought deal is selected (in order for FINRA to assess any conflicts of interest and underwriter compensation issues), but obtaining conditional clearance speeds the subsequent review process because future takedowns should not require individual approval (or additional filing fees) unless there are material changes to the original shelf filing.[28]

To the extent a filing exemption isn't available, FINRA members and non-WKSI issuers can also take advantage of FINRA's "same-day clearance" option with respect to shelf offerings. Same-day clearance filers will typically receive a no objections letter within minutes of making certain required representations through FINRA's COBRADesk filing system. FINRA does, however, reserve the right to review a transaction post filing. The same-day clearance option is available in connection with initial shelf filings, takedowns from previously approved shelf filings and initial shelf filings with concurrent takedowns (but, in each case, not if the final pro supp has been filed with the SEC). The same-day clearance option is a highly useful tool in the context of a bought deal, with one glaring limitation. The same-day clearance option is not currently available for secondary offerings. This means that even if an issuer has obtained conditional clearance on the base prospectus, FINRA does not have a process specifically established for obtaining same-day clearance for a secondary bought deal. If the deal team is faced with this situation, counsel for the selling stockholder and the underwriter are advised to reach out to the FINRA staff to discuss expediting the review process.

In order to take advantage of the same-day clearance option, issuers must agree to file the final pro supp and executed underwriting agreement with FINRA within one business day of filing the final pro supp with the SEC and must also make the following representations:

- the terms with the underwriter do not include any prohibited arrangements (as described in Rule 5110(f));
- the aggregate amount (including underwriting discounts and commissions and all other "items of value") received by the underwriter does not exceed 8 percent of the offering proceeds, and all underwriting compensation will be disclosed in the offering document;
- the underwriter has not acquired unregistered securities that would be deemed compensation during the 180-day period preceding the filing (note that, because of this requirement, the same-day clearance option may not technically be available if the underwriter or related persons have entered into a derivative transaction with the issuer in connection with the offering (even if such instrument is deemed to have "zero compensation value" under the rule));
- in the event of a Rule 5121 conflict of interest that requires the appointment of a QIU, the QIU meets all the necessary standards to act as a QIU in the subject offering (taking into account the type and size of the offering); and
- final offering documents will be submitted to FINRA.

Since non-WKSIs can avail themselves of the same-day clearance option in most instances and WKSIs have their own expedited review process, some forward thinking by the deal team with respect to the Corporate Financing Rule's review and approval requirements can help minimize FINRA as a gating item at the time of the bought deal. However,

because the same-day clearance option is not currently available in connection with a secondary offering, the deal team will need to engage in communications with FINRA in advance to discuss how the related review will impact timing. Additionally, regardless of whether same-day clearance is an option, certain representations and other information will always be required by FINRA, so the deal team will want to gather the information necessary to make the required representations as early in the process as possible.

Blue Sky Filings

It's easy to overlook the need for state securities law clearance in a bought deal. In most cases, the analysis breaks down as follows:

- *The Listed or "Senior to a Listed" Exemption*. Securities listed on a national securities exchange or securities of the same issuer that are equivalent or senior in rank to a listed security qualify as a so-called "covered security" under Section 18 of the Securities Act and have the benefit of federal preemption of any applicable filing or fee required under state securities laws. Accordingly, for bought deals that involve securities of a listed company, offers and sales can be made to all types of investors in the United States by broker-dealers registered in each applicable state without any other sort of qualification under the various states' securities laws.
- *Other Public Offerings*. If the bought deal is for securities of an issuer that does not have any securities listed on an exchange, blue sky filings will be required to sell to retail investors. Generally, if offers and sales are limited to institutional investors, an exemption from state securities registration will be available, but the breadth of this exemption varies by state. A blue sky survey is usually prepared by underwriter's counsel for these types of offerings in order to inform the underwriter of the types of investors who may participate in the offering in each state.
- *Rule 144A/Regulation S Offerings*. If the offering is to be conducted under Rule 144A to qualified institutional buyers located in the United States, an exemption from registration is available in every state if the offer and sale is made by a registered broker-dealer. State securities laws likewise do not apply to the sale of securities outside the United States under Regulation S.

Form 8-K Filings in Addition to the Launch Press Release

Generally, a Form 8-K must be filed with the SEC within four business days of the underlying event that triggers the need for disclosure. In the context of a bought deal, the deal team should consider the following potential triggering events (in addition to the launch press release discussed above):

- *Material Definitive Agreement*. Item 1.01 of Form 8-K requires a reporting company to file a Form 8-K describing the terms of any material definitive agreement it has entered into outside of the ordinary course of business. Practitioners have differing opinions as to whether the underwriting agreement associated with a bought deal is material, given the paucity of ongoing obligations post-closing.[29] If the underwriting agreement is filed, the underwriter will likely request that it be filed *after* the final pro supp is filed.
- *Unregistered Sales of Equity Securities*. A company must file a Form 8-K if it sells equity securities in a private placement or other transaction not registered under the Securities Act and the amount of securities sold since the last time the company made similar disclosure in a Form 8-K or other periodic report is greater than 1 percent of the number of shares outstanding of the class of security sold.[30] If such securities are sold for cash, then the Form 8-K must

include disclosure of the aggregate offering price and underwriting commission.

Stock Exchange Notices, Listing Approvals and Stockholder Vote Requirements

If the securities being offered in a bought deal are to be listed on either the NYSE or Nasdaq, certain exchange notices and approvals may be necessary. In addition, the exchanges require stockholder approval prior to consummating certain offerings. As a result, the deal team should focus on the NYSE and Nasdaq requirements in order to determine as early as possible whether any such notices or approvals will be necessary. However, in the context of a bought deal for common stock, stockholder approval will generally not be required under either the NYSE or Nasdaq rules to the extent the offering takes the form of a registered offering for cash that is underwritten on a firm commitment basis.[31]

The NYSE requirements are:

- *Notification and Approval to List.* NYSE-listed companies are required to file an application for the listing of additional shares. Additional shares cannot be listed until the issuer receives notification of the NYSE's approval. The NYSE suggests that all filings be made approximately two weeks prior to the time when authorization is required. While the NYSE will work with issuers to grant their authorization on a more accelerated timeframe, issuers should make this confidential filing as soon as a bought deal moves beyond a theoretical discussion, particularly if the offering requires significant analysis under the "20 Percent Rule" discussed below.
- *Stockholder Approval and the 20 Percent Rule*. Among other informational requirements, the additional listing application must indicate whether the offering requires stockholder approval and, if so, whether the required approval has been obtained. Rule 312.03(c) of the NYSE Listed Company Manual requires stockholder approval for any transactions or series of transactions where either (i) the common stock to be issued in the offering (or underlying the convertible securities to be issued in the offering) has/will have upon issuance voting power equal to or in excess of 20 percent of the voting power outstanding before the issuance or (ii) the number of shares to be issued in the offering (or underlying the convertible securities to be issued in the offering) are/will be upon issuance equal to or greater than 20 percent of the number of shares outstanding prior to the issuance. Obviously, the need to solicit advance stockholder approval typically eliminates the advantages of a bought deal. Fortunately, there are three exceptions to the NYSE's 20 Percent Rule:
  - "public offerings" for cash;
  - "bona fide private financings;"[32] and
  - offerings for distressed companies in limited circumstances.

The Nasdaq requirements are:

- *Notification.* Rule 5250(e)(2) of the Nasdaq listing rules requires the issuer of any class of securities (other than American Depositary Receipts) listed on Nasdaq to submit electronically a listing of additional shares notification in connection with certain issuances, or potential issuances, of common stock or securities convertible into common stock. The listing notification must be submitted at least 15 calendar days[33] prior to:
  - issuing any common stock (or security convertible into common stock) in connection with the acquisition of the stock or assets of another company, if any officer or director or "substantial shareholder" of the issuer has 5

percent or greater interest (or if collectively such persons have a 10 percent or greater interest) in the company to be acquired or consideration to be paid; or

- o issuing any common stock, or any security convertible into common stock in a transaction that may result in the potential issuance of common stock, greater than 10 percent of either the total shares outstanding or the voting power outstanding on a pre-transaction basis.

In addition, Rule 5250(e)(1) requires an issuer to notify Nasdaq when there is an aggregate increase or decrease of any class of its securities that exceeds 5 percent of the amount of the securities of the class outstanding. Notification is required to be filed no later than 10 calendar days after such occurrence. Nasdaq reviews these filings in order to confirm that any proposed transaction complies with the various Nasdaq listing rules, including the stockholder approval requirements described below.

- *Stockholder Approval*. Rule 5635(d) of the Nasdaq listing rules generally requires stockholder approval of transactions (other than "public offerings") involving:
  - o the sale, issuance or potential issuance by an issuer of common stock (or securities convertible into or exercisable for common stock) at a price below the greater of book or market value, which together with sales by officers, directors or "substantial shareholders," is at least 20 percent of the common stock or at least 20 percent of the voting power outstanding prior to the issuance; or
  - o the sale, issuance or potential issuance by an issuer of common stock (or securities convertible into or exercisable for common stock) equal to 20 percent or more of the common stock or 20 percent or more of the voting power outstanding before the issuance for less than the greater of book or market value of the stock.

Note that registered offerings do not necessarily constitute "public offerings" under the NYSE's and Nasdaq's rules. As a result, a fact-specific inquiry will be required and practitioners should determine early on whether stockholder approval pursuant to the NYSE's or Nasdaq's rules will be necessary. The application of the NYSE and Nasdaq rules in the context of offerings of convertible securities is particularly tricky. If you are planning a bought deal for convertible securities, this topic needs special focus prior to launch.

Conclusion

Bought deals demand speed and grace under pressure from every member of the deal team. Both underwriters and issuers are focused on completing bought deal financings before the market moves or market participants can affect the price of the issuer's securities through hedging. To accomplish this, all of the required documentation should be in final form before any underwriter bids are submitted and accepted. Remember that all of the customary issues encountered in fully marketed transactions also exist in bought deals, including all of the issues arising under SEC and FINRA rules and regulations, the NYSE and Nasdaq rules, state blue sky laws and the antifraud provisions of the federal securities laws. The only difference is that everything happens at lightning speed.

Endnotes

[1] Securities Industry and Financial Markets Association, *Block Trade Guidelines*, March 2008, available at http://www.sifma.org/uploadedfiles/for_members/committees/capital_markets_group/equity_markets(1)/sifma%20block%20trade%20guidelines%20(2008).pdf.

[2] Although a bought deal can in theory be effected pursuant to a registration statement on Form S-1, the inability to forward-incorporate reports filed by the issuer under the Securities Exchange Act of 1934, among other practical impediments, makes this an atypical structure.

[3] *See* Rule 462(e). For a review of the definition of WKSI, see our Words of Wisdom blog entry "Joining the Club: WKSIs Part 1" (February 14, 2012), available at http://www.wowlw.com/wksis/wksi-part-1/.

[4] For more information on how Rule 462(b) works for shelf upsizing, see our Words of Wisdom blog entry "'For a Few Dollars More': Upsizing Your Shelf Deal" (May 25, 2010), available at http://www.wowlw.com/shelf-offerings/for-a-few-dollars-more-upsizing-your-shelf-deal1/.

[5] Public companies with less than $75 million aggregate market value of voting and non-voting common equity held by non-affiliates (public float) are subject to an additional limitation when offering common stock. Under General Instruction I.B.6 of Form S-3, they cannot use Form S-3 to sell securities amounting to more than the equivalent of one-third of their public float during any 12 consecutive month period. Therefore, any issuer with a public float of less than $75 million will need to consider capacity with respect to this one-third offering limitation before entering into a bought deal transaction.

[6] For the issuer and the underwriter, a takedown triggers a new effective date as of the earlier of the date of first use of a pro supp filed under Rule 424(b) and the time of the first contract of sale of the securities to which the pro supp relates. A pro supp generally does not create a new effective date for the company's auditor by virtue of Rule 430B(f)(2), and accordingly there is typically no need to update the auditor's consent pursuant to Section 7 of the Securities Act. *See Securities Offering Reform*, Release No. 33-8591, text accompanying note 470 (July 19, 2005) (hereinafter, "*Offering Reform Release*").

[7] For a thorough review of the law and the lore surrounding "offers," see our *Client Alert* "The Good, the Bad and the Offer: Law, Lore and FAQs," available at http://www.lw.com/page/thegood-thebad-theoffer.

[8] *See* Rule 163(c) and note 170 to *Offering Reform Release* ("In addition, as with the other exemptions and safe harbors that are available only to the issuer, the definition of by or on behalf of the issuer [in Rule 163] explicitly excludes offering participants who are underwriters or dealers."). In 2009, the SEC proposed amendments to Rule 163(c) that would have allowed underwriters to make pre-filing offers on behalf of WKSIs, but these proposed amendments are not currently expected to be enacted.

[9] *See* Rule 100(b)(2) of Regulation FD, excluding from its requirements disclosure made "to a person who owes a duty of trust or confidence to the issuer (such as an attorney, investment banker, or accountant)" and to a person "who expressly agrees to maintain the disclosed information in confidence." Accordingly, the exception covering communications between an investment banker (a temporary insider) and an issuer is implied and, therefore, need not be expressly made.

[10] For an overview of the practical aspects of the EDGAR filing process, see our Words of Wisdom blog entries "'All About EDGAR' (and Exhibits)" (May 11, 2010), available at http://www.wowlw.com/edgar/all-about-edgar1-and-exhibits/ and "All About EDGAR, Part II–Filings: Paper or Plastic?" (May 24, 2011), available at http://www.wowlw.com/edgar/all-about-edgar-part-ii--filings-paper-or-plastic/.

[11] This limited information includes: (1) basic factual information about the issuer; (2) information about the terms of the securities offered; (3) the names and roles of participating underwriters; (4) the anticipated schedule for the offering; (5) a description of the procedures by which the underwriters will conduct the offering; (6) the names of selling security holders, if any; and (7) the exchanges on which the securities are traded. *See* Rule 134(a).

[12] Arguably, the issuance of a press release concurrently with launch is by itself sufficient to satisfy Regulation FD's simultaneous public disclosure requirement for issuers who are actively followed by the wire services. *See* Rule 101(e)(2) of Regulation FD. However, many issuers choose to concurrently file or furnish the press release on Form 8-K in order to update both the Section 11 and Section 12 files. *See* Rule 101(e)(1) of Regulation FD.

[13] WKSIs can make material changes to the plan of distribution by incorporated Exchange Act reports or prospectus supplements. *See* Rule 430B and Offering Reform Release text accompanying note 449. Non-WKSIs, however, must file a post-effective amendment if there is a material change to the plan of distribution.

[14] Section 202.05 of the NYSE's Listed Company Manual requires a listed company to "release quickly" to the public any news or information that might reasonably be expected to materially affect the market for its securities. Although the NYSE, in Section 202.01 of the Listed Company Manual, pointed to various developments that are potentially material (*e.g.*, earnings, mergers/acquisitions, securities offerings and pricings related to these offerings and major product launches), it leaves the ultimate determination of materiality, and therefore disclosure, with the listed company.

In 2011, the NYSE provided guidance on how its timely alert policy affects secondary offerings and, specifically, bought deals. The NYSE guidance provides:

> "In the case of a 'bought deal,' the materiality of a particular transaction will depend on a number of factors, including, but not limited to, the number of shares sold, the size of the discount to the public market price paid by the underwriter, and whether the transaction involves a sale by the company or one of its stockholders. If the discount to the public market price is such that its disclosure would materially affect the market for the securities, then it may be appropriate to disclose the pricing terms (or amount of securities sold and net proceeds to the company or stockholder) even if the number of shares sold in the transaction is not itself material."

[15] As a result of anticipated downward pressure on the price of the stock following launch, the difference between the price the underwriter pays for the shares and the last closing price does not necessarily represent the effective compensation to the underwriter.

[16] For a discussion of the practical and legal issues surrounding disclosure of recent results, see our *Client Alert* "Recent Developments In Recent Developments — Using 'Flash' Numbers in Securities Offerings," available at http://www.lw.com/page/flash-numbers-securities-offerings.

[17] Sellers of common stock are most likely to explore a private investment in public equity, or PIPE, in this context. A common stock PIPE involves the private sale to accredited investors typically coupled with resale registration rights with respect to the purchased shares. Would-be underwriters of a bought deal may act as placement agents in this context.

[18] Bear in mind that, under Rule 144A(d)(3)(i), debt securities convertible into common stock with an effective conversion premium of less than 10 percent are treated as fungible with securities of the class into which they are convertible. In other words, in that case, if the exemption under Rule 144A is unavailable for the common stock, it would similarly be unavailable for the convertible debt.

[19] Note that FINRA is currently proposing new filing and disclosure obligations on certain private placements in which a FINRA member participates. Fortunately, the proposed rules have several exemptions, including placements to qualified institutional buyers and offerings under Rule 144A and Regulation S. *See Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; Notice of Filing of Partial Amendment No. 1 and Order Instituting Proceedings to Determine Whether to Approve or Disapprove a Proposed Rule Change, as modified by Partial Amendment No. 1, to Adopt FINRA Rule 5123 (Private Placements of Securities) in the Consolidated FINRA Rulebook* Release No. 34-66203 (Jan. 20, 2012).

[20] In contrast to Sections 11 and 12 of the Securities Act, *scienter* is required to establish liability under Rule 10b-5 of the Exchange Act.

[21] Pursuant to Rule 101(c)(1) of Regulation M, an "actively-traded security" includes securities with an average daily trading volume of at least $1 million and that are issued by an issuer whose common equity securities have a public float value of at least $150 million.

[22] In some cases, the ***absence*** of a lock-up may be material information that the deal team should consider including in the Section 12 file, particularly where investors would expect to see a lock-up based on market practice or prior experience with the issuer.

[23] Rule 139 requires, among other things, that the issuer in question be eligible to conduct primary offerings under General Instruction I.B.1 of Form S-3 (*e.g.*, meets the $75 million minimum public float requirement) and that the publication in question is not an initiation or re-initiation of research coverage (*i.e.*, that the report is a continuation of regularly published reports on the issuer).

[24] Other exemptions include certain offerings involving non-convertible debt and preferred securities, most private placements and certain exchange offers in which listed securities are issued.

[25] *See* FINRA Rule 5110(b)(7)(C)(i).

[26] One scenario in which the filing of the takedown may not be required in this instance is if the issuer filed the original shelf at a time when no FINRA member was involved (this is because the Corporate Financing Rule's filing requirement is technically triggered only when a FINRA member is participating in the offering). Nonetheless, because FINRA's procedures with regard to shelf filings are subject to change, it is best practice to assess the situation at the time to determine whether a FINRA filing will be necessary.

[27] *See* FINRA Rule 5121(f)(5) and (6) for a definition of "Conflict of Interest" and "Control," respectively.

[28] FINRA filings made in connection with the filing of a shelf registration statement (whether filed by issuer's or underwriters' counsel) must include a representation that the maximum amount of underwriting compensation in connection with offerings off the shelf will not exceed 8 percent of the maximum offering proceeds. Such

representation must also appear in the base prospectus included in the shelf registration statement.

One item of note with respect to FINRA Rule 5121 is that the definition of "conflict of interest" for purposes of that rule relates to a FINRA member's participation in "an entity's public offering." However, the defined term "entity" in Rule 5121 excludes "a 'real estate investment trust' as defined in Section 856 of the Internal Revenue Code." While this exclusion doesn't exempt a REIT from FINRA filing requirements alone, it does effectively mean that a conflict of interest as defined for purposes of Rule 5121 cannot exist in the context of an offering by a REIT. As a result, conditional clearance of the base prospectus by a REIT by and large only leaves underwriter compensation for FINRA review at the time of a subsequent takedown.

[29] *See SEC Division of Corporation Finance, Compliance and Disclosure Interpretations,* Exchange Act Form 8-K, Question 102.02. Some issuers choose to file the underwriting agreement as an exhibit under Item 9.01 of Form 8-K. By doing so, the issuer can incorporate the terms of the underwriting agreement by reference into Item 1.01 and provide a more limited summary of the terms of the agreement. However, the issuer may also choose to wait and file the underwriting agreement as an exhibit to its next quarterly or annual Exchange Act filing covering the period during which the bought deal occurred.

[30] For smaller reporting companies (as defined by the SEC), the threshold is increased to greater than 5 percent (as opposed to 1 percent) of the number of shares outstanding of the class of security sold.

[31] Although a "public offering" for cash is exempted from the stockholder approval requirements of NYSE Rule 312.03, the NYSE Listed Company Manual does not include a definition of "public offering" for the purposes of assessing this exemption. Nasdaq Rule 5635(d) also exempts "public offerings" from the stockholder approval requirements of the Nasdaq Listing Rules. However, Nasdaq has also provided additional guidance on what constitutes a "public offering" for the purposes of Rule 5635(d): "Generally, a firm commitment underwritten securities offering registered with the Securities and Exchange Commission will be considered a public offering for these purposes. . . . However, Nasdaq staff will not treat an offering as a 'public offering' for purposes of the shareholder approval rules merely because they are registered with the Commission prior to the closing of the transaction." Nasdaq Listing Rules, IM-5635-3, "Definition of a Public Offering."

[32] Rule 312.04(g) of the NYSE Listed Company Manual defines a "bona fide private financing" to include a sale in which "a registered broker-dealer purchases the securities from the issuer with a view to the private sale of such securities to one or more purchasers." Accordingly, an exempt bought deal will generally qualify for this exception.

[33] While Rule 5250(e)(2) of the Nasdaq listing rules specifies that the listing notification must be submitted 15 calendar days prior to the issuance of the applicable securities, in practice Nasdaq staff has been receptive to the concern that, in many cases, complying with this advance notice requirement is impossible, given that the offering may only become a reality a few days (or a single day) prior to the date the securities are issued and sold. Accordingly, Nasdaq staff will often accommodate the submission of the listing notification inside of this 15-day window. However, the deal team should reach out to Nasdaq as soon as they become aware of a possible offering and offer to submit a draft notification in advance. Constant communication with Nasdaq will generally assist in facilitating greater flexibility with respect to the 15-day window.

Annex A

Note: This timeline is based on the assumption that there will be one week between the first phone call and the launch date. In many cases, the schedule will be significantly accelerated. In those cases, the to-do list will not change, but the timeline will need to be compressed. Good luck!

Sample Timeline for a Registered Bought Deal

FIVE BUSINESS DAYS PRIOR TO TRADE DAY:

- Issuer engages its own counsel and designated underwriter's counsel
- Check for an effective shelf registration statement (with sufficient unused capacity to cover green shoe) and no stop-order
- Determine whether stock exchange filings/stockholder approvals are needed
- Submit FINRA filing (if required) and request pre-clearance for trade day
- Submit stock exchange filing (if required)
- Contact auditors to initiate the comfort letter process
- Instruct underwriter's counsel to begin its due diligence process

FOUR BUSINESS DAYS PRIOR TO TRADE DAY:

- Issuer's counsel circulates drafts for comment to underwriter's counsel of the:
  - o Preliminary prospectus supplement
  - o Launch press release*
  - o Pricing press release
  - o Underwriting agreement
  - o Form of lock-up agreement (if an equity offering)
  - o Authorizing resolutions of the board of directors
  - o Any other transaction documentation
- Underwriter's counsel updates its due diligence

TWO/THREE BUSINESS DAYS PRIOR TO TRADE DAY:

- Issuer's counsel reaches out to potential underwriters to confirm agreement as to confidentiality and wall-crossing procedures
- Issuer conducts a call with potential underwriters to discuss process and timing for solicitation of final bids
- Underwriter's counsel completes its documentary due diligence
- Potential underwriters contact underwriter's counsel to receive an up-to-date diligence download
- All underwriter comments on the relevant transaction documents are submitted and resolved
- Final form of comfort letter is circulated, negotiated and agreed

TRADE DAY:

- The underwriter hosts a bring-down due diligence call with counsel, the issuer and its auditor
- Final bids are submitted immediately after the close of trading
- A winning underwriter is selected
- Issue launch press release (and file or furnish it on Form 8-K)
- File preliminary pro supp with SEC
- Provide a pdf of preliminary pro supp to underwriters
- Commence public sales and begin to confirm orders
- Execute the underwriting agreement,** lock-up agreements and the auditor's comfort letter

* See SIFMA's Block Trade Guidelines for recommended forms of launch press releases for common stock deals.

** In some cases, the underwriting agreement is not executed until the next morning.

TRADE DAY +1:

- Continue confirming orders***
- Issue press release announcing clearing price if a primary fixed price offering (before the market opens)
  - o Notify stock exchange prior to issuing press release
- Execute and overnight stock powers and medallion guarantees to transfer agent
- Notify stock exchange about intention to list additional shares (if applicable)

TRADE DAY +2:

- File final prospectus supplement with the SEC pursuant to Rule 424(b) at the close of business
- Assemble execution versions of closing documents, bring down comfort letter, various officer's certificates and legal opinions

CLOSING (TRADE DAY +3):

- Hold bring-down due diligence call
- Close offering
- File Form 8-K

*** In a "sticky" deal, confirmation of orders may continue for multiple days. In this case, the deal team will need to be mindful of Rule 159 and Registration M issues.

If you have any questions about this *Client Alert*, please contact one of the authors listed below or the Latham attorney with whom you normally consult:

Senet S. Bischoff
+1.212.906.1834
senet.bischoff@lw.com
New York

Brandon J. Bortner
+1.202.637.2117
brandon.bortner@lw.com
Washington, D.C.

Alexander F. Cohen
+1.202.637.2284
alexander.cohen@lw.com
Washington, D.C.

Kirk A. Davenport II
+1.212.906.1284
kirk.davenport@lw.com
New York

Dana G. Fleischman
+1.212.906.1220
dana.fleischman@lw.com
New York

Joel H. Trotter
+1.202.637.2165
joel.trotter@lw.com
Washington, D.C.

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