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SEC Permits All Issuers to Engage in “Test-the-Waters” Communications

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The Securities and Exchange Commission (the “SEC”) has adopted new Rule 163B under the Securities Act of 1933, as amended (the “Act”), to permit all issuers, or any person authorized to act on behalf of an issuer, to gauge market interest in a registered securities offering through discussions with potential investors that are, or that the issuer or person to act on its behalf reasonably believes are, “qualified institutional buyers” (as defined in Rule 144A under the Act) or institutional “accredited investors” (as defined in Rule 501 under the Act) prior to or following the filing of a registration statement. Rule 163B will become effective 60 days after publication in the Federal Register.

Available to All Issuers

Prior to the adoption of Rule 163B, only emerging growth companies (“EGCs”) and their authorized representatives were allowed to engage in “test-the-waters” communications pursuant to Section 5(d) of the Act, which was added as part of the JOBS Act. Rule 163B is available to all issuers, including non-reporting companies, EGCs, non-EGCs, well-known seasoned issuers, and investment companies (including registered investment companies and business development companies).

Status of Test-the-Waters Communications Under the Rule

Section 5(c) of the Act prohibits any written or oral offers of a security prior to the filing of a registration statement. Once a registration statement is filed, Section 5(b)(1) of the Act limits written offers to a “statutory prospectus” that conforms to the information requirements of Section 10 of the Act.

Under Rule 163B, communications that comply with the Rule will be exempt from Section 5(b)(1) and Section 5(c) of the Act, but would constitute an “offer” subject to potential liability

under Section 12(a)(2) of the Act as well as the anti-fraud provisions of federal securities laws. Section 12(a)(2) of the Act imposes liability on sellers for offers or sales made orally or through a prospectus that includes an untrue statement of material fact or omits to state a material fact that makes the statements made, in light of the circumstances under which they were made, not misleading. In the release adopting Rule 163B (the “Adopting Release”), the SEC also cautioned issuers that information provided in a test-the-waters communication must not conflict with material information in the related registration statement.

No Filing or Legending Requirements

Communications under Rule 163B are not required to be filed with the SEC and are not required to include any specific legend. A communication under Rule 163B will not constitute a free writing prospectus as defined in Rule 405 under the Act, and the SEC has clarified that a similar communication by an emerging growth company under Section 5(d) of the Act also is not a free writing prospectus. However, consistent with its practice in reviewing registration statements filed by EGCs, in connection with its review of a registration statement, the SEC or its staff can request an issuer to furnish any test-the-waters communications used in connection with an offering.

Regulation FD Considerations

In the Adopting Release, the SEC cautioned that issuers subject to Regulation FD need to consider whether any information in the test-the-waters communication would trigger disclosure obligations under Regulation FD or whether an exception to disclosure under Regulation FD would apply.

Impact of Rule 163B Communications on Flip to Private Placement

In response to commentator concerns, the SEC stated in the Adopting Release that whether a test-the-waters communication would constitute a "general solicitation" under Regulation D would depend on the facts and circumstances under which the communication was conducted. The SEC also clarified that if an issuer chooses to engage in test-the-waters communication under Rule 163B concurrently with communications related to a private offering, it can conduct such communications in a manner that preserves the availability of both Rule 163B and any offering exemption upon which it might otherwise rely for the private placement.

Nonexclusive Safe Harbor

Rule 163B is being adopted as a "nonexclusive" safe harbor. Issuers will continue to be able to rely on other communications rules under the Act or other available exemptions when determining how, when, and what to communicate in connection with a contemplated securities offering.

For Further Information

The Adopting Release can be found at <https://www.sec.gov/rules/final/2019/33-10699.pdf>. Clients with questions on Rule 163B should contact Jack Hogoboom at 973-597-2382 (jhogoboom@lowenstein.com) or any other member of our Capital Markets & Securities Group.

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