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LEXOLOGY®
Getting The Deal Through

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Lexology Getting The Deal Through is delighted to publish the eighteenth edition of *Securities Finance*, which is available in print and online at www.lexology.com/gtdt.

Lexology Getting The Deal Through provides international expert analysis in key areas of law, practice and regulation for corporate counsel, cross-border legal practitioners, and company directors and officers.

Throughout this edition, and following the unique Lexology Getting The Deal Through format, the same key questions are answered by leading practitioners in each of the jurisdictions featured. Our coverage this year includes new chapter on Switzerland.

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Every effort has been made to cover all matters of concern to readers. However, specific legal advice should always be sought from experienced local advisers.

Lexology Getting The Deal Through gratefully acknowledges the efforts of all the contributors to this volume, who were chosen for their recognised expertise. We also extend special thanks to the contributing editors, Mark Greene, Andrew Pitts and George Stephanakis of Cravath, Swaine & Moore LLP, for their continued assistance with this volume.

LEXOLOGY
Getting The Deal Through

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United States

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LEGAL AND REGULATORY FRAMEWORK

Laws and regulations

1 | What are the relevant statutes and regulations governing securities offerings?

Two statutes primarily govern the US securities markets at the federal level: the Securities Act of 1933 (the Securities Act), which was designed to regulate offerings of securities to the public, and the Securities Exchange Act of 1934 (the Exchange Act), which was designed to regulate subsequent trading of those securities in secondary market transactions. These statutes regulate the securities markets through disclosure requirements as opposed to any requirements for regulatory approval of the merits of an offering.

The Securities Act requires that every offer and sale of a security in the United States be registered with the Securities and Exchange Commission (SEC) unless an exemption is available (eg, offers and sales not involving a public offering). The Securities Act has two basic objectives: to provide investors with material financial and other information regarding the issuer and the securities to be offered, and to prevent fraud in connection with sales of securities.

To achieve these objectives, the Securities Act requires that, in the absence of an exemption, a statutory prospectus that has been filed with the SEC as part of the registration process be provided in advance to purchasers of securities, and imposes statutory liability for material omissions or misstatements in those documents or in any other documents that may be provided to purchasers under the Securities Act.

The Exchange Act requires US and non-US companies with a security listed on a US stock exchange (including the New York Stock Exchange and NASDAQ), meeting certain asset amounts and shareholder number requirements, or making public offerings of securities in the United States, to register such securities with the SEC and to file with the SEC annual reports, quarterly reports (in the case of US companies) and certain other reports containing information similar to that required in a registration statement under the Securities Act.

On 5 April 2012, the United States adopted a capital formation reform bill known as the Jumpstart Our Business Startups Act (the JOBS Act). The JOBS Act significantly eases restrictions under the Securities Act relating to the initial public offering process for equity securities of a newly designated class of smaller companies and to the private placement capital raising process for virtually all issuers. The JOBS Act also provides ongoing relief, mainly for smaller companies, from certain requirements under the Exchange Act as well as from certain existing (and potentially future) accounting and auditing rules.

Offerings of securities are also subject to state 'blue sky' laws, although the federal National Securities Markets Improvement Act of 1996 has largely pre-empted state securities laws.

In addition, companies that complete a securities offering that is registered with the SEC or otherwise become subject to the reporting obligations of the Exchange Act must comply with the provisions of the Sarbanes-Oxley Act of 2002, including the provisions with respect to internal control over financial reporting; prohibitions on loans made to executive officers and directors; requirements relating to auditor independence and independent audit and compensation committees; certifications by executive officers of financial reports; and increased civil and criminal penalties for violations of the securities laws. Those companies must also comply with the Dodd–Frank Wall Street Reform and Consumer Protection Act of 2010, which introduced important changes to the corporate governance and executive compensation landscape for public companies.

Regulator

2 | Which regulatory authority is primarily responsible for the administration of those rules?

The SEC is the primary administrative authority charged with administering the Securities Act, the Exchange Act and the other federal securities laws. In addition to enforcing these statutes, the SEC is charged with promulgating rules and regulations thereunder.

PUBLIC OFFERINGS

Mandatory filings

3 | What regulatory or stock exchange filings must be made in connection with a public offering of securities? What information must be included in such filings or made available to potential investors?

Unless an exemption from the registration process is available, an issuer must file a registration statement with the Securities and Exchange Commission (SEC) before any offers to sell securities may be made or solicitations of offers to buy securities may be done by the issuer or underwriters (other than 'testing the waters' communications), and the registration statement must be declared effective by the SEC before the securities may be sold. The information required to be included in the registration statement is intended to provide investors with all material information about the offering as well as the business and financial condition of the issuer.

To facilitate disclosure of material information about the issuer and the offering, the SEC promulgated Regulation S-K (governing disclosure generally) and Regulation S-X (governing financial disclosure), which codify the disclosure requirements for registration statements filed under the Securities Act, regardless of whether the offered security is debt or equity or the offering is primary or secondary.

Subject to certain conditions, financial statements of non-US issuers may be prepared in accordance with International Financial Reporting Standards, as issued by the International Accounting Standards Board without the need for reconciliation to US generally accepted accounting principles.

The Jumpstart Our Business Startups Act (the JOBS Act) eases certain of these registration requirements for emerging growth companies (EGCs), entities that issue or propose to issue any security, and that have less than US$1.07 billion in total annual gross revenues and meet certain other requirements. EGCs are granted relief from, among other things, certain financial disclosures required in a common equity IPO registration statement, and may elect to have the registration statement confidentially reviewed by the SEC before its use. In 2017, the SEC extended these confidential review procedures to all issuers.

In addition to registering the securities with the SEC, an issuer generally applies for listing of equity securities (and some debt securities) on a US securities exchange. To be listed on a US securities exchange, it is also necessary to register the securities under the Exchange Act, which can generally be accomplished with a short-form filing under the Exchange Act incorporating the Securities Act filings made with respect to the offering of such securities. In addition, the relevant exchange application usually requires certain undertakings from the issuer that it meets the minimum standards for listing. Those listing standards vary for different types of equity and debt securities.

Review of filings

4 What are the steps of the registration and filing process? May an offering commence while regulatory review is in progress? How long does it typically take for the review process to be completed?

Section 5 of the Securities Act effectively divides the registration process into three periods: the pre-filing period, the waiting period and the post-effective period.

The pre-filing period is the period between the time there is an agreement or understanding between the issuer or seller and the underwriters to issue or sell securities and the filing of the registration statement. During the pre-filing period, which typically begins 30 to 45 days before the filing of the registration statement, offers to sell or solicitations of offers to buy securities, other than offers or solicitations by well-known seasoned issuers (WKSIs) and testing the waters communications, are prohibited under the Securities Act.

The waiting period is the period between the filing of the registration statement and when it is declared effective by the SEC. Until the registration statement is declared effective, it is unlawful under the Securities Act to sell the securities that are the subject of the registration statement. However, offers made orally or pursuant to a preliminary prospectus or free-writing prospectus (meeting the requirements of the Securities Act) are permitted. Offers made by television, radio, internet or any sort of written notice, circular, advertisement, letter or communication in writing not meeting the requirements of a preliminary prospectus or free-writing prospectus under the Securities Act are impermissible during the waiting period. Accordingly, during the waiting period, underwriters and certain executive officers of the issuer normally commence a 'roadshow' during which they distribute a preliminary prospectus and make oral presentations to potential investors. While on the roadshow, which can last up to several weeks, the underwriters also begin obtaining non-binding indications of interest from potential investors, enabling them to judge the level of investor interest and set an appropriate offering price for the securities.

The length of the waiting period varies according to several factors. A registration statement relating to an issuer's IPO will almost always be selected by the SEC for a full review, whereas registration statements relating to more frequent issuers and secondary offerings are less likely to be reviewed. In addition, the particular industry of the issuer and the presence of any 'hot-button' issues in the registration statement may increase the chances of SEC review. If a registration statement is selected for full review, the SEC will generally review it for approximately 30 days before issuing a comment letter containing questions and requests for additional or supplemental information. Depending on the number and the nature of the SEC comments, issuers are generally able to respond and clear comments within three to six weeks following receipt of the initial SEC comment letter. Once comments are clear, the issuer can request effectiveness from the SEC.

The post-effective period is the period after the registration statement has been declared effective by the SEC. During this time, the securities registered under the registration statement may be sold so long as the security or, in most instances, the confirmation of sale that is delivered to the purchaser, is preceded by a filing with the SEC of a final prospectus meeting the requirements of the Securities Act. Once the registration statement has been declared effective, the issuer and underwriters will negotiate the final terms of the offering based on the indications of interest solicited during the roadshow as well as other factors, and a final prospectus containing pricing information will be filed with the SEC and may be printed and sent to investors along with final sales confirmations.

In 2005, the SEC substantially altered the registration and communication framework applicable to public offerings. Among the most significant changes was the creation of WKSIs, comprising companies with a worldwide public float of US$700 million or that have issued US$1 billion of non-convertible debt securities in registered primary offerings for cash in the past three years. WKSIs are entitled to a flexible registration and communication regime, particularly with respect to 'shelf' registration statements. Shelf registration statements, once effective, allow issuers to make continuous or delayed offerings of registered securities. Shelf registration statements filed by WKSIs become automatically effective upon filing with the SEC and are subject to minimal incremental disclosure requirements. Another significant change is that the SEC now permits issuers, subject to certain conditions, to use free-writing prospectuses after and, in the case of WKSIs, before filing a registration statement with the SEC. Free-writing prospectuses are written communications, including electronic communications, that constitute offers of securities other than statutory prospectuses filed with the SEC.

Publicity restrictions

5 What publicity restrictions apply to a public offering of securities? Are there any restrictions on the ability of the underwriters to issue research reports?

Offers of any kind made before the filing of a registration statement, and written offers made other than by a preliminary prospectus or a free-writing prospectus during the waiting period, are violations of section 5 of the Securities Act. Because 'offer' is defined to include 'every attempt or offer to dispose of, or solicitation of an offer to buy . . . for value', and prospectus is defined to include any 'notice, circular, advertisement, letter, or communication, written or by radio or television', issuers and underwriters must carefully monitor all publicity about the issuer or the proposed offering to avoid running afoul of the Securities Act.

Notwithstanding the provisions of section 5 of the Securities Act, the SEC has issued several rules to permit limited publicity relating to the issuer and the offering during the pre-filing and waiting periods. Before filing a registration statement, an issuer may publicly disclose in a press release that it intends to make a public offering of securities, provided that release contains only limited information (such as the name of the issuer and the title, amount and basic terms of the securities to be offered). The underwriters may not be named. In addition, communications by issuers more than 30 days before filing a registration statement are not considered prohibited offers, provided they do not reference a securities offering and issuers take reasonable steps to prevent further distribution or publication of those communications during the 30-day period preceding the filing of a registration statement. The SEC also allows reporting issuers (but not other offering participants, including underwriters) to continue publishing regularly released factual business information and forward-looking information, but without referencing an offering. In addition, WKSIs are permitted to make oral offers and use free-writing prospectuses even before a registration statement is filed. During the period after a registration statement is filed but before it is declared effective, the issuer can also advertise the offering through a 'tombstone ad' that complies with the Securities Act rules. Those advertisements are also restricted to certain basic information about the issuer and the offering, but may include the names of the managing underwriters.

The JOBS Act created a new exemption under section 5 of the Securities Act to allow 'testing the waters' communications with certain investors. The new exemption permits EGCs and their representatives to engage in oral and written communications with potential investors that are qualified institutional buyers (QIBs) (as defined in rule 144A under the Securities Act) or institutions that are accredited investors (as defined in Regulation D under the Securities Act) to determine whether those investors 'might have an interest in a contemplated securities offering' at any time regardless of whether the issuer has filed a registration statement. In 2019, the SEC extended the ability to use testing the waters communications to all issuers.

Research reports

In the absence of any exemptions, research reports would clearly constitute illegal prospectuses under section 5 of the Securities Act. Restrictions on the issuance of research reports are generally more stringent in IPOs. Underwriters, however, often conduct research on public companies and issue reports in the ordinary course of their business. To avoid hampering such ordinary course activities, the SEC has adopted rules allowing the limited publication of research reports during the course of an offering. These rules allow an investment bank that publishes research in the ordinary course of its business to continue to do so, provided the investment bank is not participating in the distribution of the issuer's securities and does not receive consideration in connection with the publication of such information from that issuer or any other persons interested in the distribution. In addition, these rules allow a participating underwriter to publish research reports with respect to an issuer that is a reporting company under the Exchange Act, so long as such underwriter has been doing so in the regular course of its business.

The JOBS Act eased certain of these restrictions concerning research activities by investment banks with respect to EGCs. Among other relief, the JOBS Act provides that a broker or dealer is permitted to publish or distribute a research report about an EGC that is the subject of the proposed public offering of common equity, even if the broker or dealer participates in the offering.

Secondary offerings

6 Are there any special rules that differentiate between primary and secondary offerings? What are the liability issues for the seller of securities in a secondary offering?

Contrary to the securities laws of several European countries, there are no special rules differentiating primary and secondary offerings in the United States. Pre-emptive rights in the United States are rare and the US securities laws do not contemplate any special rules where these rights exist. Also generally absent from the corporate laws of the individual states are laws that, for example, require state approval for the issuance of shares or impede the ability of issuers to indemnify selling stockholders such that would necessitate special rules differentiating primary and secondary offerings.

Settlement

7 What is the typical settlement process for sales of securities in a public offering?

The SEC has adopted a rule mandating that, by default, a purchase of securities in a public offering settle two business days after the date of the contract of sale (unless the securities were priced after 4.30pm Eastern Standard Time, in which case the settlement date may be three business days after the date of the contract of sale). However, the rule provides that the parties to a sale transaction may agree to a longer or shorter settlement cycle, which may be accomplished by including notice of the alternative settlement cycle in the related offering documentation. For securities listed on an exchange, the requirements of the relevant exchange may make a longer settlement cycle difficult to implement.

PRIVATE PLACINGS

Specific regulation

8 Are there specific rules for the private placing of securities? What procedures must be implemented to effect a valid private placing?

Yes, section 4(a)(2) (formerly 4(2)) of the Securities Act exempts 'transactions by an issuer not involving any public offering'. A substantial body of case law and Securities and Exchange Commission (SEC) regulatory practice has developed concerning private placements under section 4(a)(2). The availability of the exemption turns on a factual analysis of several factors, including the number and sophistication of the offerees, the relationship between the issuer and the offerees, the minimum denomination of the securities being offered and the relative bargaining power between the issuer and the offerees. To ensure compliance with section 4(a)(2), issuers often have purchasers make certain representations as to their sophistication as investors and their receipt of all requisite information in connection with the offering.

To provide issuers with certainty regarding the section 4(a)(2) exemption, the SEC adopted Regulation D, which provides three regulatory exemptions from the registration requirements of the Securities Act for offers and sales by issuers. Rule 504 of Regulation D provides exemptions from the registration requirements of the Securities Act for certain securities offerings limited in aggregate dollar amount (eg, offerings not exceeding US$10 million, depending on the parameters of the offering). Rule 506 of Regulation D (by far the most widely used Regulation D exemption) provides issuers with a nonexclusive, 'unlimited' safe harbour under section 4(a)(2) of the Securities Act, that exempts offerings of an unlimited amount of securities to an unlimited number of 'accredited investors' (eg, institutions and certain wealthy individuals) and to no more than 35 non-accredited investors. The previous prohibition on general solicitation and advertising in Rule 506 offerings was eliminated by rules adopted by the SEC pursuant to the JOBS Act. The relevant rule changes allow general advertising and solicitation in Rule 506 offerings as long as all purchasers are accredited investors. In an offering made under Regulation D (subject to narrow exceptions), the issuer must exercise reasonable care to ensure that the purchasers are not taking the securities with a view to distribution or other resale.

The primary method of offering high-yield debt securities in the United States is through a section 4(a)(2) private placement by the issuer to financial intermediaries, immediately followed by a resale of such securities to QIBs pursuant to Rule 144A under the Securities Act, in offshore transactions pursuant to Regulation S under the Securities Act, or using both methods.

As required by the JOBS Act, the SEC adopted amendments that took effect in June 2015, which created a new exemption from registration pursuant to section 3(b) of the Securities Act for up to US$75 million of securities (Regulation A+). Under another requirement of the JOBS Act, the SEC adopted rules that took effect in May 2016, which created a substantial regulatory framework providing for a crowdfunding exemption from registration, whereby small aggregate amounts of securities of an issuer can be sold through brokers or internet 'funding portals' to investors in small individual accounts.

Investor information

9 | What information must be made available to potential investors in connection with a private placing of securities?

If a sale is made to a non-accredited investor, Regulation D requires that certain information be provided to the purchaser within a reasonable time before the sale. The information to be provided varies according to whether the issuer is a reporting company under the Exchange Act, but in either case such information is similar to that which would be required in a registration statement in the case of a registered offering under the Securities Act. Regulation D does not require that any specific information be provided to accredited investors. Nonetheless, in practice, issuers generally provide potential purchasers with information similar to that provided to non-accredited investors.

In addition, Rule 144A and Regulation S have limited information requirements. However, issuers offering securities via section 4(a)(2) private placements coupled with resales pursuant to rule 144A and Regulation S typically provide information that is similar to what would be required in a registration statement in the case of a registered offering under the Securities Act.

Transfer of placed securities

10 | Do restrictions apply to the transferability of securities acquired in a private placing? And are any mechanisms used to enhance the liquidity of securities sold in a private placing?

Yes. Unregistered securities purchased in a private placement may not be resold except pursuant to a registration statement under the Securities Act or an exemption contained in the Securities Act or the rules and regulations thereunder. Several mechanisms exist to facilitate the resale of these 'restricted' securities.

One such mechanism is the 'section 4(1-1/2)' exemption, now '4(a) (1-1/2)', which allows investors who purchased restricted securities in a valid private placement to resell those securities in a further private placement following the procedures set forth in section 4(a)(2) without being deemed an underwriter engaged in a distribution of securities (who would not be exempt from the registration requirements of section 5 of the Securities Act). In December 2015, section 4(a)(7) to the Securities Act was adopted; this exemption essentially codifies the '4(a)(1-1/2)'exemption.

The most commonly used mechanism for resales of restricted securities that are listed on a stock exchange is Rule 144 under the Securities Act. Rule 144 defines the circumstances under which an owner of restricted securities or an affiliate of the issuer may offer and sell those securities to the public without being deemed an underwriter engaged in a distribution of securities. Rule 144 provides a non-exclusive safe harbour for the resale of restricted securities of a reporting issuer beginning six months after issuance of those securities, subject to requirements as to the public availability of certain information regarding the issuer and, in the case of resales by affiliates only, to limitations as to the manner and volume of those sales. With respect to the restricted securities of a non-reporting issuer, Rule 144 provides a non-exclusive safe harbour for resales beginning one year after issuance of those securities. Under Rule 144, after a one-year holding period, public resales of restricted securities of reporting and non-reporting issuers may be made by non-affiliates without any restriction.

Another important mechanism for reselling restricted securities is pursuant to Rule 144A under the Securities Act. Rule 144A permits an investment bank or other financial intermediary who has purchased restricted securities from an issuer in a private placement to make resales of those securities to an unlimited number of qualified institutional buyers (QIBs) without being deemed an underwriter engaged in a distribution of securities. Generally, QIBs consist of large institutions that own or invest on a discretionary basis, in aggregate, at least US$100 million in securities of unaffiliated issuers. Sales under rule 144A can take place immediately after a valid private placement under section 4(a)(2), and securities acquired by QIBs pursuant to rule 144A are deemed restricted securities for the purposes of the resale restrictions. Rule 144A may not be used to offer securities that are fungible with (ie, of the same class as) a listed security, and therefore it is not available in connection with equity offerings (other than offerings of convertible securities with a conversion premium of at least 10 per cent) of companies whose shares are listed on a US stock exchange.

Historically, the exemption under rule 144A only has been available if both offers and sales were made only to QIBs. Effective September 2013, rules adopted by the SEC pursuant to the JOBS Act allow offers to non-QIBs in rule 144A offerings, as long as sales are made only to QIBs.

Finally, Regulation S under the Securities Act enhances liquidity for holders of restricted securities by allowing them to resell restricted securities in offshore transactions.

OFFSHORE OFFERINGS

Specific regulation

11 | What specific domestic rules apply to offerings of securities outside your jurisdiction made by an issuer domiciled in your jurisdiction?

The Securities and Exchange Commission has adopted Regulation S to provide an exemption from the registration requirements for securities offered and sold outside the United States. Regulation S provides a safe harbour from the registration requirements of the Securities Act for offers and sales by issuers, distributors and their respective affiliates and resales by persons other than issuers, distributors and their respective affiliates. In general, for an offer or sale of securities to qualify for Regulation S, the offer or sale must be made in an offshore transaction and neither the issuer nor any distributor may engage in any 'directed selling efforts' in the United States. Permissible selling efforts in connection with a concurrent US offering do not constitute directed selling efforts that preclude reliance on Regulation S for a non-US offering.

For an offer or sale of securities to be made in an offshore transaction, the offer may not be made to a person in the United States and, at the time the buy order is originated, either the purchaser must be outside the United States (or the seller must reasonably believe that the purchaser is outside the United States) or the transaction must take place on a physical trading floor of an established foreign securities exchange located outside the United States. In practice, Regulation S permits US investors who purchase unregistered securities of a non-US issuer, among other things, to resell those securities in the non-US market in which those securities principally trade.

To sell restricted securities under the safe harbour provided by Regulation S, sellers must meet certain other requirements that vary according to the type of issuer. In general, these additional requirements are less burdensome when it is less likely that the securities will flow back to the US market (category 1) and more burdensome when there is an actual or potential substantial US market for the issuer's securities (category 3). When adequate information about the issuer is publicly available in the United States, the concerns about securities flowing into the US market are somewhat reduced, and the restrictions fall between the two extremes (category 2).

PARTICULAR FINANCINGS

Offerings of other securities

12 | What special considerations apply to offerings of exchangeable or convertible securities, warrants or depositary shares or rights offerings?

Convertible securities

An offering of any convertible security, whether convertible debt or warrants, raises the question of what procedures, if any, must be adopted to ensure that the issuance of the underlying securities upon conversion is exempt from the registration requirements of the Securities Act. In most cases, no additional procedures are required because section 3(a)(9) of the Securities Act exempts from the registration requirements of the Securities Act the issuance of securities upon conversion of other securities of the same issuer.

However, this exemption does not apply if a commission or other remuneration is paid or given directly or indirectly for soliciting such exchange, or where the underlying security is that of a different issuer from the issuer of the convertible security (unless the issuer of the underlying security fully and unconditionally guarantees obligations of the issuer of the convertible security in respect of such convertible security). Accordingly, if the section 3(a)(9) exemption is unavailable, the issuer must either register the underlying securities or issue such securities pursuant to an exemption from the registration requirements of the Securities Act.

Exchangeable securities

Mandatorily exchangeable securities involve the issuance by one issuer of a debt security that is mandatorily exchangeable at its maturity into common stock of a different issuer (or the cash equivalent of that common stock). If the common stock is restricted or the issuer of the mandatorily exchangeable securities is an affiliate of the issuer of the common stock, both the mandatorily exchangeable securities and the common stock must be registered to consummate a public offering of the mandatorily exchangeable securities; otherwise, the underlying common stock need not be registered to conduct a public offering of the mandatorily exchangeable securities (provided that the prospectus for the mandatorily exchangeable securities includes certain information concerning the issuer of the common stock unless that issuer meets certain registration eligibility and listing criteria).

Depositary shares

In lieu of issuing securities directly to US investors, a non-US issuer may establish an American depositary receipt programme whereby the non-US issuer deposits its outstanding securities with the foreign correspondent of a US commercial bank and the US commercial bank issues to the US investors securities (American depositary shares (ADSs)) representing the deposited securities (the physical certificates representing those ADSs are referred to as American depositary receipts (ADRs)). The Securities and Exchange Commission (SEC) allows non-US issuers to set up, with the assistance of US depositary banks, over-the-counter ADR programmes for shares already outstanding without a need to register the ADRs or the underlying shares under the Exchange Act if the non-US issuer agrees to provide the SEC with certain required material information that it makes publicly available in its home country. However, if the ADRs are listed on a US stock exchange, both the ADRs and the underlying securities must be registered under the Exchange Act, which subjects the non-US issuer to the SEC reporting and disclosure requirements and to the provisions of the Sarbanes-Oxley Act of 2002. Also, public offerings of ADRs in the United States must be registered under the Securities Act.

Rights offerings

In 1999, the SEC enacted a rule exempting from the registration requirements of the Securities Act certain rights offerings of non-US issuers. The primary conditions to the exemption are that, at the time of the rights offering, US security holders own no more than 10 per cent of the securities that are the subject of the rights offering, and that the US security holders are permitted to participate in the rights offering on terms at least as favourable as those offered to the other holders of the securities that are the subject of the rights offering. In addition, the securities offered in the rights offering must be equity securities of the same class as those held by the offerees in the United States directly or through ADRs.

UNDERWRITING ARRANGEMENTS

Types of arrangement

13 | What types of underwriting arrangements are commonly used?

Public securities offerings in the United States are generally made through a syndicate of underwriters led by one or more managing underwriters. The underwriting agreement defines the relationship between the underwriters and the issuer and is the document pursuant to which the underwriters commit to purchase the securities that are the subject of the offering. The underwriters typically agree to purchase the securities two business days after the pricing date. In contrast to the practices in many other countries, the underwriters' commitments to purchase securities pursuant to the underwriting agreement are always several rather than joint-and-several. This practice reflects the limitation of liability of an underwriter under section 11 of the Securities Act to the total offering price of the securities that it underwrites.

Typical provisions

14 | What does the underwriting agreement typically provide with respect to indemnity, force majeure clauses, success fees and overallotment options?

Indemnity

The issuer will covenant in the underwriting agreement to indemnify the underwriters (and their officers, directors, agents and controlling persons) against all liabilities and expenses arising out of alleged misstatements or omissions in the registration statement, the prospectus and any free writing prospectuses and roadshow materials, excluding certain minor portions for which the underwriters assume responsibility. Because of existing legal uncertainty as to the enforceability of such indemnity provisions, underwriting agreements also usually provide that if indemnification is held by a court to be unavailable, the issuer and the underwriters will share aggregate losses in such proportion as is appropriate to reflect the relative fault for the misstatement or omission giving rise to the loss, the relative benefits received by the issuer and the underwriters from the offering of the securities (with the liability of each underwriter being capped by the underwriting discount or commission received by such underwriter in respect of the sale of such securities), or both the losses and benefits.

Force majeure

Underwriting agreements in US offerings also routinely contain force majeure and termination clauses permitting the underwriters to terminate their obligations under the underwriting agreement if, in their judgement, there has been a sharp downturn in market conditions or deterioration of the financial condition or business of the issuer between the signing of the underwriting agreement and the scheduled closing of the offering such that consummating the offering would be impracticable. Typical force majeure clauses also extend to the occurrence of natural disasters or calamities, such as an outbreak of hostilities or suspension of trading in the United States or, in certain cases, non-US securities markets. Underwriters tend to view the unilateral right to declare a force majeure event and to terminate as a fundamental protection provided to them in the underwriting agreement. Nonetheless, force majeure clauses in US offerings are rarely exercised by the underwriters, principally because of the limited period of time between the signing of the underwriting agreement and the closing of the offering (typically two business days) and the potential reputational harm associated with an underwriter's exercise of those clauses.

Overallotment

Because it is customary in US offerings to authorise the managing underwriters to over-allot (ie, to offer and sell more securities than the underwriters have contracted to purchase from the issuer), it is also customary in the underwriting agreement to provide the underwriters with an 'overallotment option' allowing them to purchase from the issuer at the public offering price (less commission) up to an additional 15 per cent of the securities being offered to cover such overallotments. The overallotment option is more commonly found in equity offerings (and equity-linked offerings such as convertible debt) than in debt offerings.

Success fees

These are rare in US offerings because of the unique liability provisions of the Securities Act. Section 11(e) of the Securities Act limits the liability of an underwriter to the total price at which the securities underwritten by it and distributed to the public were offered. However, if any underwriter receives from the issuer some benefit, direct or indirect, for its services that is not shared proportionately with the other underwriters, then such an underwriter forfeits this limitation on liability. As a result, success fees are generally avoided by underwriters.

Other regulations

15 | What additional regulations apply to underwriting arrangements?

Several rules and regulations of the Financial Industry Regulatory Authority (FINRA) apply to underwriting arrangements in registered securities offerings. Subject to a number of exemptions depending on the class of security and the particular offering, FINRA will review the underwriting agreement and certain other offering documentation governing the underwriting arrangements prior to an offering to ensure that the terms of such agreements and arrangements are fair and reasonable. FINRA also requires that any overallotment option be limited to 15 per cent or less of the securities being offered. FINRA places limits on the amount of total compensation that any underwriter can receive in connection with an offering, as well as on participation by any underwriter with certain conflicts of interest in respect of the offering (eg, if the issuer will use offering proceeds to repay a loan from an affiliate of an underwriter). FINRA also imposes several limitations on the allocation of securities and other distribution practices, particularly in 'hot issues' in which demand for the securities is high, the market price of the offered securities rises after pricing and potential abuses are considered more likely to occur.

ONGOING REPORTING OBLIGATIONS

Applicability of the obligation

16 | In which instances does an issuer of securities become subject to ongoing reporting obligations?

An issuer may become subject to the ongoing reporting obligations of the Exchange Act in a variety of circumstances. For instance, any issuer that has a class of securities listed on a US securities exchange is subject to the reporting requirements of the Exchange Act. These requirements apply for both debt and equity securities, regardless of whether the security has been publicly offered in the United States. US companies are also required to become reporting companies if they have US$10 million or more of assets at the end of a fiscal year and a class of equity securities held by 2,000 or more persons, or 500 or more persons who are not accredited investors. For banks, bank holding companies and savings and loan holding companies, the separate trigger for equity securities held by 500 or more non-accredited persons does not apply.

The same is true for non-US companies, provided that at least 300 of the holders of the class of equity securities are resident in the United States and the company has not claimed, or is not eligible for, the rule 12g3-2(b) reporting exemption under the Exchange Act. Rule 12g3-2(b) provides that qualifying non-US companies that would otherwise be subject to the reporting requirements of the Exchange Act owing to the number of US holders of their securities may instead provide (in English) certain information that the company makes public pursuant to the laws of its home country, distributes to its security holders or files with any stock exchange on which its securities are listed. To qualify for rule 12g3-2(b), the subject class of securities must have a 'primary trading market' outside of the United States. A primary trading market can be either a single non-US exchange where at least 55 per cent of the average daily trading volume in the subject class of securities occurred during the company's most recently completed fiscal year or two exchanges that, when combined, satisfy the same requirement, provided that at least one has a greater average trading volume in the subject class of securities than the United States.

Finally, if an issuer has issued US-registered securities, it must file Exchange Act reports for any year in which there are 300 or more holders (or, in the case of a non-US company, 300 or more US holders) of those registered securities (excluding the fiscal year in which the registration statement for those securities was declared effective, during which Exchange Act reports must be filed regardless of the number of holders).

Information to be disclosed

17 | What information is a reporting company required to make available to the public?

The information a registrant must make available to the public pursuant to the Exchange Act is substantially similar to that an issuer must file with the SEC in the context of a public offering of securities, reflecting a policy decision by the Securities and Exchange Commission (SEC) that the information needed to make an informed investment decision is similar in the context of both purchases in a public offering and purchases in the secondary market. Based on this belief, the SEC has implemented an integrated disclosure system to achieve substantial uniformity of disclosure in filings under the Securities Act and the Exchange Act, including disclosure regarding the issuer's business, legal status, results of operations and financial condition. The Jumpstart Our Business Startups Act (the JOBS Act) provides relief to emerging growth companies (EGCs) for certain reporting and disclosure obligations, such as 'say on pay' votes and some executive compensation-related disclosures. Additionally, EGCs are exempted from auditor attestation requirements with respect to internal control over financial reporting under section 404 of the Sarbanes-Oxley Act of 2002 and may elect to omit selected financial data for any period prior to the earliest period for which audited financial statements were presented in their IPO registration statement.

ANTI-MANIPULATION RULES

Prohibitions

18 | What are the main rules prohibiting manipulative practices in securities offerings and secondary market transactions?

Regulation M is the primary collection of rules in the United States on market manipulation and stabilisation, with the primary intent of preventing interested parties from engaging in activities that could artificially raise the price of a security in an offering. These rules generally prohibit underwriters and broker-dealers participating in the offering of a security, as well as issuers and selling security holders, from purchasing (or inducing others to purchase) the securities they are selling in the offering (with certain exceptions, most notably for actively traded securities) as well as specified 'reference' securities. Under Regulation M, persons conducting short sales within a specified time prior to the pricing of an offering are generally prohibited from purchasing in that offering.

Financial Industry Regulatory Authority (FINRA) rules also aim to prevent certain manipulative practices. FINRA rules on 'free-riding and withholding' are intended, in the case of 'hot issues' where the price in the secondary market is higher than the public offering price, to ensure that all the securities in the offering are sold at the initial public offering price. The Papilsky Rules adopted by FINRA are also intended to ensure that all the offered securities are sold at the public offering price without direct or indirect discounts, selling concessions or other allowances except as disclosed in a prospectus.

PRICE STABILISATION

Permitted stabilisation measures

19 | What measures are permitted in your jurisdiction to support the price of securities in connection with an offering?

Stabilising activities in connection with an offering are permitted, provided that persons initiating stabilising bids do so with reference to the independent prices in the principal market for the security and such bids do not exceed either the independent bid or the offering price of the security.

LIABILITIES AND ENFORCEMENT

Bases of liability

20 | What are the most common bases of liability for a securities transaction?

There are several common bases of liability for violating federal securities laws in a securities transaction. Under section 12(a)(1) of the Securities Act, parties who improperly offer or sell securities in violation of section 5 of the Securities Act are strictly liable to the purchaser regardless of whether that purchaser's loss was related to the violation. Recovery under section 12(a)(1) is limited to either rescission or, if the plaintiff no longer owns the security, to monetary damages in an amount equal to the difference between the purchase price and the sale price of the securities.

Section 11 of the Securities Act imposes liability on, among others, an issuer, its directors and the underwriters when a registration statement contains an untrue statement of a material fact or omits to state a material fact necessary to make the included statements not misleading. A fact is 'material' if there is a substantial likelihood that a reasonable purchaser would consider that fact to be important in making his or her investment decision. If misstatements or omissions exist, any purchaser may bring a civil suit, and he or she need not prove either a causal relationship between the material misstatement or omission and the decline in value or that he or she relied on the misstatement or omission in purchasing the security. The plaintiff is also not required to prove intent on the part of the defendant. Under section 11, the defendants may escape liability by proving that the plaintiffs knew of the disclosure deficiency when purchasing the security. Defendants (other than the issuer) also have an affirmative 'due diligence' defence under section 11 whereby they can escape liability by showing that, after reasonable investigation, they had reasonable grounds to believe that the information contained in the registration statement was true and that nothing was omitted. With respect to the 'expertised' portions of the registration statement (eg, the audited financial information of the issuer), affirmative diligence is not required – defendants need merely show that they had no reasonable ground to believe, and did not believe, that there was a material misstatement or omission at the time of effectiveness. The *WorldCom* decision, *In re WorldCom, Inc Securities Litigation*, 346 F. Supp. 2d 628 (SDNY 2004), has introduced some uncertainty into the distinction between 'expertised' and 'non-expertised' portions of the registration statement for purposes of the due diligence defence. A plaintiff who prevails on section 11 grounds is entitled to monetary damages equal to the difference between the price paid for the securities (but not greater than the public offering price) and the price of the securities at the time of suit or the price at which the plaintiff disposed of the securities.

Another basis for liability in securities transactions is section 12(a)(2) of the Securities Act, which provides that any person who offers or sells a security by means of any oral or written communication that contains an untrue statement of a material fact, or omits to state a material fact necessary to make the included statements not misleading, is liable to the purchaser for damages. As under section 11, the plaintiff is not required to prove intent, but the plaintiff must show that he or she was not aware of the misstatement or omission and that the misstatement or omission somehow affected his or her decision to purchase the securities. Section 12(a)(2) liability extends only to those who offer and sell the securities, though courts have interpreted this to include officers, directors and principal stockholders of the issuer, where those persons authorise the promotional efforts of the underwriters and help prepare the offering and other selling documents. The Securities and Exchange Commission (SEC) has also confirmed that issuers of securities constitute 'sellers' under section 12(a)(2), regardless of the form of underwriting arrangement entered into. Defendants have an affirmative defence if they can prove that they did not know, and reasonably could not have known, of such misstatement or omission. Unlike under section 11, defendants do not have a duty to investigate to invoke the affirmative defence under section 12(a)(2). Plaintiffs who still own the securities are entitled to rescission. Plaintiffs who no longer own the securities are limited to recovering damages actually caused by the misstatements or omissions. Section 12(a)(2) liability attaches at the time an investor becomes committed to purchase securities and enters into a contract of sale (ie, when the investor makes the investment decision). Therefore, information conveyed after the contract of sale (eg, in a subsequently delivered final prospectus) would not be considered in evaluating section 12(a)(2) liability.

Additionally, section 15 of the Securities Act provides that any person who controls any other person who is liable under either section 11 or 12 of the Securities Act will also be liable, jointly and severally, to the same extent as the controlled person (unless the controlling person had no knowledge of, or no reasonable ground to believe in the existence of, the facts that allegedly make the controlled person liable).

Private placements and unregistered secondary market transactions do not trigger either section 11 or section 12(a)(2) liability. Instead, the anti-fraud provisions of the Exchange Act and Rule 10b-5 provide the basis for liability for material misstatements and omissions in such transactions. In contrast with section 11 and section 12(a)(2), however, Rule 10b-5 requires the plaintiff to prove that the defendant had intent to defraud, deceive or manipulate investors, and that the plaintiff relied on the defendant's wrongful conduct in purchasing the security.

Although Rule 10b-5 also applies to registered offerings, the heightened burdens for establishing liability under it generally result in plaintiffs relying instead on Securities Act liability claims in such offerings. Similar to claims under sections 11 and 12(a)(2), however, claims under Rule 10b-5 can be brought against the issuer, its officers and directors, the underwriters and anyone else who directly or indirectly committed the fraud. Plaintiffs who prevail on claims relying on Rule 10b-5 may generally recover out-of-pocket losses. As with section 12(a)(2), liability under Rule 10b-5 attaches at the time an investor becomes committed to purchase securities and enters into a contract of sale.

Whether section 10(b) of the Exchange Act and Rule 10b-5 promulgated thereunder apply extraterritorially has been at issue in recent years. In Morrison v National Australia Bank, 561 US 247 (2010), the US Supreme Court reversed lower court precedent by holding that section 10(b) applies only to securities fraud in transactions in securities listed on a US exchange and to transactions in any other security that occur in the United States. Though the Morrison test was intended to clarify extraterritorial reach, lower courts continue to grapple with its application and, due to a jurisdictional provision in the Dodd–Frank Wall Street Reform and Consumer Protection Act of 2010 (Dodd–Frank), Morrison's applicability to regulatory proceedings remains unsettled.

Amendments to the securities laws as part of Dodd–Frank empowered the SEC to bring 'aiding and abetting' enforcement actions, previously available only under the Exchange Act, under the Securities Act, the Investment Advisers Act of 1940 and the Investment Company Act of 1940. Dodd–Frank did not, however, provide a private cause of action for aiding and abetting claims, though it did require the Government Accountability Office (GAO) to conduct a study concerning what effect introducing such a cause of action might have. The GAO report sets forth arguments for and against authorising such a cause of action, but did not offer a conclusion or recommendation on the advisability of doing so. To date, no such legislation has been proposed or adopted, and US courts continue to reject liability claims predicated on aiding and abetting.

21 | What are the main mechanisms for seeking remedies and sanctions for improper securities activities?

Civil litigation

Civil litigation may be brought by private parties (typically in the form of class action lawsuits), the SEC or other government agencies.

Private party plaintiffs generally seek to recover losses suffered as a result of the defendants' conduct. These private rights of action arise from express statutory provisions granting plaintiffs those rights or judicially created rights of action. Private party plaintiffs may also seek injunctive relief to compel, or more likely to enjoin, certain actions by the defendants. Government agencies typically seek forfeiture of illegally gotten gains, civil monetary penalties or injunctive relief.

Administrative proceedings

Administrative proceedings may be brought by the SEC or other relevant government agencies pursuant to rules promulgated by those agencies and before administrative law judges that the SEC or government agencies employ. In particular, in an administrative proceeding the SEC can impose monetary civil penalties and obtain cease-and-desist orders mandating immediate cessation of improper activities. These administrative proceedings are subject to limited appellate court review. In 2018, the US Supreme Court decided *Lucia v SEC*, 138 S. Ct. 2044 (2018), holding that the way the SEC appointed its administrative law judges was unconstitutional. The SEC promptly took steps to cure the deficiency and has resumed hearings before its administrative law judges.

Criminal prosecutions

Criminal proceedings based on federal securities laws may be instituted only by the US Department of Justice, though often based on the advice and recommendation of the SEC. Defendants subject to such criminal actions face potentially substantial fines and, in the case of individuals, imprisonment. At the direction of Dodd–Frank, the US Sentencing Commission promulgated in April 2012 amendments to the sentencing guidelines for financial fraud to take into account 'the potential and actual harm to the public and the financial markets resulting from the offences'. The amendments, which provide for increased penalties for certain fraud offences, took effect in November 2012. Dodd–Frank also extended the statute of limitations for securities fraud from five to six years.

Additionally, Dodd–Frank created an expansive whistle-blower regime that provides significant financial incentives for individuals who know of a potential federal securities laws violation to come forward and that protects those individuals from employer retaliation. Under final rules adopted by the SEC in May 2011 to implement the whistle-blower programme (and subject to certain limitations), if an individual voluntarily comes forward with original information about potential violations of the federal securities laws that leads to a successful enforcement action resulting in sanctions exceeding US$1 million, that individual will receive an award equal to 10 to 30 per cent of the aggregate monetary recovery. Dodd–Frank also grants protection to whistle-blowers and others who assist SEC investigations by providing them with a private right of action against retaliating employers. Remedies include reinstatement, double back pay and attorneys' fees.

UPDATE AND TRENDS

Proposed changes

22 | Are there current proposals to change the regulatory or statutory framework governing securities transactions?

Cognisant of the development of new data processing and communication technology, the Securities and Exchange Commission (SEC) continued its efforts to modernise the regulatory framework governing securities transactions with a focus on efficiency and effectiveness. The SEC released amendments that have or will become effective in the first half of 2021. Amendments that have or will impact the regulatory framework governing securities transactions include the modernisation amendments of regulations S-X, S-K and National Market System, the Market Data Infrastructure and the Electronic Data Gathering, Analysis and Retrieval system.

In addition to modernisation efforts, the SEC took action to facilitate and simplify capital formation in private markets, improve the efficiency and transparency of the whistle-blower programme and approve NYSE's proposed rule change that allows for primary direct floor listing.

23 **What emergency legislation, relief programmes and other initiatives specific to your practice area has your state implemented to address the pandemic? Have any existing government programmes, laws or regulations been amended to address these concerns? What best practices are advisable for clients?**

The SEC adjusted quickly to the changes brought on by the coronavirus. Besides maintaining the continuity of the agency operations while transitioning to telework, the SEC assembled a cross-divisional working group to monitor the market for real and potential effects of the coronavirus on various types of market participants, including the public companies, issuers, investment companies and public accounting firms.

The SEC has also responded to the coronavirus by providing pandemic-specific guidance on securities law obligations, operations, liquidity and capital resources disclosures of companies, as well as targeted regulatory assistance and extensive relief, including extending reporting and filing deadlines and accommodations to address market participants' operational difficulties associated with the coronavirus. Additionally, the Division of Enforcement of the SEC has been actively monitoring the market for new frauds, illicit schemes and other misconduct related to the coronavirus – it suspended trading in securities of over 30 issuers who made various representations related to the coronavirus and opened over 150 investigations related to covid-19.

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