PROSKAUER ROSE LLP®

Client Alert

A report for clients and friends of the Firm

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Registered Direct Securities Offerings – An Effective Financing Alternative for a Turbulent Market

Given the turbulence in today's capital markets and the generally depressed United States and global economies, many public company issuers have been searching for viable capital-raising methods after finding that both traditional public offerings and private investment in public equity (PIPE) offerings currently may not be feasible. For many issuers, a Registered Direct securities offering can be an effective alternative to raise capital. Registered Direct offerings can benefit public companies by allowing them to quickly raise capital from a select group of investors, while avoiding the significant downward pricing pressure that typically accompanies a traditional underwritten offering. At the same time, Registered Direct offerings provide investors with registered stock that is immediately tradable and, therefore, more liquid than in PIPE offerings.

The purpose of this Client Alert is to generally describe the Registered Direct offering process and to summarize the advantages of Registered Direct offerings that issuers and their investment bankers and financial advisers should consider in analyzing their capital-raising alternatives.

Overview and Advantages of a Registered Direct Offering

A Registered Direct offering is a negotiated sale by an issuer to one or more investors of securities that have been registered pursuant to an effective shelf registration statement on Form S-3 under Rule 415 of the Securities Act of 1933, as amended. Rule 415 permits an issuer to register a specific dollar or share amount of securities without specifying the amount of any particular class or type of security or the timing or method of the offering. The issuer may then sell any or all of the registered securities directly to investors at a later date or dates of its choosing. Unlike a typical firm commitment underwritten offering, a Registered Direct offering is structured as a "best efforts" offering. Accordingly, it involves a "placement agent" as opposed to an "underwriter" who places the securities directly with investors, rather than directly purchasing the securities itself and then reselling them to investors. However, similar to an underwritten offering, the issuer in a Registered Direct offering sells registered securities that generally have no restrictions on resale. Registered Direct offerings typically are for common stock, although issuers may sell other types of securities (*e.g.*, convertible notes or warrants), and often do in combination with each other.

The majority of Registered Direct offerings involve the use of a placement agent. A placement agent experienced in Registered Direct offerings typically has longstanding relationships with a number of institutional investors, along with knowledge of what industry(ies) or niche(s) a particular investor prefers to invest in and its investment criteria. Therefore, rather than marketing securities to a large group of potential investors, an experienced placement agent is able to target a small number of investors that are particularly well suited for a specific issuer and offering. Targeted investors often will include an issuer's existing institutional shareholders, other institutional shareholders of the issuer's comparable group of companies and/or traditional institutional investors who regularly purchase securities in Registered Direct offerings. Also, by interposing a placement agent between the issuer and investors, the identity of the issuer can be kept confidential until an investor is brought "over-the-wall" and informed that the offering is confidential, so that the investor is restricted from trading in the issuer's securities until the offering is completed or terminated.

The mechanics of a Registered Direct offering may present issuers and investors with important advantages over other forms of financings. For example, Registered Direct offerings typically are marketed confidentially, without any prior public announcement of the offering. This allows an issuer and its placement agent to gauge the market's interest in a financing without the downside pricing pressure that often accompanies an announced public offering. Registered Direct offerings typically are marketed based only upon an issuer's existing public disclosure. Accordingly, the issuer and placement agent, and their respective counsel, do not have to spend hours or days crafting a preliminary prospectus supplement as a selling document.

Unlike PIPE offerings, the securities purchased in Registered Direct offerings are registered, which provides immediate liquidity (subject to market conditions) that, in today's market, is of utmost importance to many investors. This advantage also runs to the issuer insofar as offering registered securities allows the issuer to offer its equity without the steep discounts to market price that often accompany PIPE offerings in the current market. Accordingly, the Registered Direct offering process provides eligible issuers with a fast, confidential and efficient financing alternative, while providing investors a managed transaction and a liquid security.

Registered Direct Offerings Are Available to a Broad Range of Public Companies

Registered Direct offerings may be conducted by small- and mid-cap public companies, as well as large-cap and Well-Known Seasoned Issuers[1], or *WKSIs*; *provided, however,* that the issuer is eligible to use Form S-3. Form S-3 (and its analogous Form F-3 for foreign issuers) is the most simplified registration form. It may only be used, however, by an issuer that has been required to report under the Securities Exchange Act of 1934, as amended, for a minimum of 12 months, and has met the filing and other requirements set forth in Form S-3's general instructions.

The use of Form S-3 confers significant advantages over other registration forms.[2] For example, Form S-3 permits the registration of securities prior to planning any specific offering and, once the registration statement is effective, issuers utilizing Form S-3 may offer securities in one or more tranches without awaiting further SEC action. In addition, Form S-3 is an "evergreen" form of registration statement – that is, it permits an issuer to incorporate by reference its reports filed with the SEC subsequent to its initial filing. Without this ability, an issuer would have to file a new registration statement or post-effective amendment to its registration statement to prevent information contained therein from becoming outdated, each of which carries the potential for SEC review and the resulting delay.

Prior to January 28, 2008, issuers seeking to utilize Form S-3 were required to have a minimum non-affiliate public float of at least $75 million for primary offerings. However, on December 19, 2007,[3] the SEC amended the eligibility requirements for the use of Form S-3 (and Form F-3) as part of its initiatives to increase access to the capital markets by smaller public companies. The amended Form S-3/F-3 eligibility rules provide many smaller public companies increased flexibility to conduct limited public offerings of their securities at times and under conditions that are best suited for them, with fewer regulatory requirements; *provided, however,* that an issuer with a public float under $75 million may not sell more than 33.33% (one-third) of its public float in primary offerings over any period of 12 calendar months. The amended rules provide additional flexibility to smaller business issuers, so that they may sell registered securities under an effective shelf registration pursuant to Rule 415 when market conditions permit, and make it easier for smaller business issuers to raise money in a Registered Direct offering. With this added flexibility, there may not be a need to conduct a PIPE offering to raise capital, which, under current market conditions, may be priced at a substantial discount to the issuer's market price due to liquidity risks.

Advantages in Registered Direct Offerings for Well-Known Seasoned Issuers

Special advantages are available in Registered Direct offerings for WKSIs, as only they can take advantage of the streamlined shelf registration process, which provides automatic effectiveness of the registration statement upon filing. These include (i) no SEC review of a WKSI's shelf registration statement, (ii) the option to pay registration fees upon only the amount of securities offered (a pay-as-you-go methodology, as opposed to payment on an entire shelf), and (iii) generally not being subject to the gun-jumping rules to which other issuers are subject. Thus, WKSIs have the unique advantage of being able to conduct a Registered Direct offering in the most confidential manner possible today. Further, if an issuer qualifies as a WKSI, it is possible to file a registration statement, market and price an offering in the same day under the appropriate circumstances.

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1 A Well-Known Seasoned Issuer is defined as a company that has timely filed its Securities Exchange Act of 1934 filings for the previous 12 months and either has a (i) worldwide public common equity float of at least $700 million (i.e., by non-affiliates) or (ii) registered and issued at least $1 billion in debt or non-convertible securities for cash (not exchange) within the prior 3 years.

2 The advantages conferred by Form S-3 also are applicable to foreign issuers via the use of Form F-3.

3 The SEC amendment became effective on January 28, 2008.

Registered Direct Offerings are Specialized Offerings

While Registered Direct offerings provide numerous advantages for public companies over other forms of capital-raising structures, they do involve a number of important business and legal issues not encountered in PIPE offerings or traditional firm commitment underwritings. Although Registered Direct offerings are not underwritten and may be marketed similarly to PIPE offerings, they are still considered public offerings under the Securities Act, and the placement agent has underwriter's liability under Section 11 of the Securities Act.[4] Accordingly, the placement agent(s) in Registered Direct offerings should conduct customary due diligence, use a placement agency and subscription agreement that includes representations, warranties and indemnities, and require delivery of a comfort letter, legal opinion, 10b-5 statement and other customary closing documents. Since all of these actions must be completed on an extremely expedited basis and the documents must be specifically tailored for a Registered Direct offering, as opposed to a traditional underwritten offering, it is important for issuers and placement agents in Registered Direct offerings to be well prepared going into the process.

Proskauer Rose LLP is one of the leading law firms in the area of Registered Direct offerings, as well as other forms of alternative capital market transactions, and has extensive experience in matters relating to structuring Registered Direct offerings, disclosure issues, marketing issues, closing mechanics, the relevant FINRA rules and regulations, rules relating to placement agent compensation, shareholder approval, the structuring and valuation of warrants in combination with other equity securities and the use of free writing prospectuses, as well as the analysis of NASDAQ, NYSE and AMEX rules, regulations and staff interpretations.

For the year ended 2008, in the category of "Placement Agent Counsel," Proskauer was nationally ranked 1st by "Placement Tracker" for the aggregate dollar amount placed, and 2nd by both "Placement Tracker" and "PrivateRaise" for the number of offerings represented. Proskauer was also tied for 4th place in 2008 in "Placement Tracker's" national rankings in the representation of investors for the number of PIPE offerings.

For further information, please feel free to contact the partners listed below or your usual contact at Proskauer.

[4] Section 11 of the Securities Act of 1933 imposes civil liability for misstatements or omissions of material facts in a securities offering registration statement. Potential Section 11 defendants include the issuer, directors, underwriters and accountants.

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Proskauer's Capital Markets Group has extensive experience in all types of capital markets transactions, including both registered and exempt transactions. We represent domestic and foreign private issuers and underwriters in registered transactions and exempt Rule 144A, Regulation S and Regulation D transactions. We provide the full range of services required by our domestic and international clients to facilitate initial public offerings, follow-on offerings, investment-grade, convertible and high-yield debt offerings and real estate securities transactions.

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