that is no longer an issuer described in paragraph (i)(1)(i), then those securities may be sold subject to the requirements of this section after one year has elapsed from the date that the issuer filed "Form 10 information" with the Commission.

(3) The term "Form 10 information" means the information that is required by Form 10 or Form 20-F (§ 249.210 or § 249.220f of this chapter), as applicable to the issuer of the securities, to register under the Exchange Act each class of securities being sold under this rule. The issuer may provide the Form 10 information in any filing of the issuer with the Commission. The Form 10 information is deemed filed when the initial filing is made with the Commission.

Rule 144A. Private Resales of Securities to Institutions.

Preliminary Notes:

1. This section relates solely to the application of Section 5 of the Act and not to antifraud or other provisions of the federal securities laws.

2. Attempted compliance with this section does not act as an exclusive election; any seller hereunder may also claim the availability of any other applicable exemption from the registration requirements of the Act.

3. In view of the objective of this section and the policies underlying the Act, this section is not available with respect to any transaction or series of transactions that, although in technical compliance with this section, is part of a plan or scheme to evade the registration provisions of the Act. In such cases, registration under the Act is required.

4. Nothing in this section obviates the need for any issuer or any other person to comply with the securities registration or broker-dealer registration requirements of the Securities Exchange Act of 1934 (the "Exchange Act"), whenever such requirements are applicable.

5. Nothing in this section obviates the need for any person to comply with any applicable state law relating to the offer or sale of securities.

6. Securities acquired in a transaction made pursuant to the provisions of this section are deemed to be "restricted securities" within the meaning of Rule 144(a)(3) of this chapter.

7. The fact that purchasers of securities from the issuer thereof may purchase such securities with a view to reselling such securities pursuant to this section will not affect the availability to such issuer of an exemption under section 4(a)(2) of the Act, or Regulation D under the Act, from the registration requirements of the Act.

(a) *Definitions.*

(1) For purposes of this section, *qualified institutional buyer* shall mean:

(i) Any of the following entities, acting for its own account or the accounts of other qualified institutional buyers, that in the aggregate owns and invests on a discretionary basis at least $100 million in securities of issuers that are not affiliated with the entity:

(A) Any *insurance company* as defined in section 2(a)(13) of the Act;

Note: A purchase by an insurance company for one or more of its separate accounts, as defined by Section 2(a)(37) of the Investment Company Act of 1940 (the "Investment Company Act"), which are neither registered under Section 8 of the Investment Company Act nor required to be so registered, shall be deemed to be a purchase for the account of such insurance company.

(B) Any *investment company* registered under the Investment Company Act or any *business development company* as defined in Section 2(a)(48) of that Act;

(C) Any *Small Business Investment Company* licensed by the U.S. Small Business Administration under section 301(c) or (d) of the Small Business Investment Act of 1958 or any *Rural Business Investment Company* as defined in section 384A of the Consolidated Farm and Rural Development Act;

(D) Any *plan* established and maintained by a state, its political subdivisions, or any agency or instrumentality of a state or its political subdivisions, for the benefit of its employees;

(E) Any *employee benefit plan* within the meaning of Title I of the Employee Retirement Income Security Act of 1974;

(F) Any trust fund whose trustee is a bank or trust company and whose participants are exclusively plans of the types identified in paragraph (a)(1)(i)(D) or (E) of this section, except trust funds that include as participants individual retirement accounts or H.R. 10 plans.

(G) Any *business development company* as defined in Section 202(a)(22) of the Investment Advisers Act of 1940;

(H) Any organization described in section 501(c)(3) of the Internal Revenue Code, corporation (other than a bank as defined in section 3(a)(2) of the Act or a savings and loan association or other institution referenced in section 3(a)(5)(A) of the Act or a foreign bank or savings and loan association or equivalent institution), partnership, limited liability company, or Massachusetts or similar business trust;

(I) Any *investment adviser* registered under the Investment Advisers Act; and

(J) Any institutional accredited investor, as defined in rule 501(a) under the Act (17 CFR 230.501(a)), of a type not listed in paragraphs (a)(1)(i)(A) through (I) or paragraphs (a)(1)(ii) through (vi).

Note 1 to Paragraph (a)(1)(i)(J): An entity seeking qualified institutional buyer status under Rule 144A(a)(1)(i)(J) may be formed for the purpose of acquiring the securities being offered under this section.

(ii) Any *dealer* registered pursuant to Section 15 of the Exchange Act, acting for its own account or the accounts of other qualified institutional buyers, that in the aggregate owns and invests on a discretionary basis at least $10 million of securities of issuers that are not affiliated with the dealer, *provided* that securities constituting the whole or a part of an unsold allotment to or subscription by a dealer as a participant in a public offering shall not be deemed to be owned by such dealer;

(iii) Any *dealer* registered pursuant to Section 15 of the Exchange Act acting in a riskless principal transaction on behalf of a qualified institutional buyer;

Note. A registered dealer may act as agent, on a non-discretionary basis, in a transaction with a qualified institutional buyer without itself having to be a qualified institutional buyer.

(iv) Any investment company registered under the Investment Company Act, acting for its own account or for the accounts of other qualified institutional buyers, that is part of a family of investment companies which own in the aggregate at least $100 million in securities of issuers, other than issuers that are affiliated with the investment company or are part of such family of investment companies. "Family of investment companies" means any two or more investment companies registered under the Investment Company Act, except for a unit investment trust whose assets consist solely of shares of one or more registered investment companies, that have the same investment adviser (or, in the case of unit investment trusts, the same depositor), Provided That, for purposes of this section:

(A) Each series of a series company (as defined in Rule 18f-2 under the Investment Company Act [17 CFR 270.18f-2]) shall be deemed to be a separate investment company; and

(B) Investment companies shall be deemed to have the same adviser (or depositor) if their advisers (or depositors) are majority-owned subsidiaries of the same parent, or if one investment company's adviser (or depositor) is a majority-owned subsidiary of the other investment company's adviser (or depositor);

(v) Any entity, all of the equity owners of which are qualified institutional buyers, acting for its own account or the accounts of other qualified institutional buyers; and

(vi) Any *bank* as defined in Section 3(a)(2) of the Act, any savings and loan association or other institution as referenced in Section 3(a)(5)(A) of the Act, or any foreign bank or savings and loan association or equivalent institution, acting for its own account or the accounts of other qualified institutional buyers, that in the aggregate owns and invests on a discretionary basis at least $100 million in securities of issuers that are not affiliated with it and that has an audited net worth of at least $25 million as demonstrated in its latest annual financial statements, as of a date not more than 16 months preceding the date of sale under the rule in the case of a U.S. bank or savings and loan association, and not more than 18 months preceding such date of sale for a foreign bank or savings and loan association or equivalent institution.

(2) In determining the aggregate amount of securities owned and invested on a discretionary basis by an entity, the following instruments and interests shall be excluded: bank deposit notes and certificates of deposit; loan participations; repurchase agreements; securities owned but subject to a repurchase agreement; and currency, interest rate and commodity swaps.

(3) The aggregate value of securities owned and invested on a discretionary basis by an entity shall be the cost of such securities, except where the entity reports its securities holdings in its financial statements on the basis of their market value, and no current information with respect to the cost of those securities has been published. In the latter event, the securities may be valued at market for purposes of this section.

(4) In determining the aggregate amount of securities owned by an entity and invested on a discretionary basis, securities owned by subsidiaries of the entity that are consolidated with the entity in its financial statements prepared in accordance with generally accepted accounting principles may be included if the investments of such subsidiaries are managed under the direction of the entity, except that, unless the entity is a reporting company under Section 13 or 15(d) of the Exchange Act, securities owned by such subsidiaries may not be included if the entity itself is a majority-owned subsidiary that would be included in the consolidated financial statements of another enterprise.

(5) For purposes of this section, *riskless principal transaction* means a transaction in which a dealer buys a security from any person and makes a simultaneous offsetting sale of such security to a qualified institutional buyer, including another dealer acting as riskless principal for a qualified institutional buyer.

(6) For purposes of this section, *effective conversion premium* means the amount, expressed as a percentage of the security's conversion value, by which the price at issuance of a convertible security exceeds its conversion value.

(7) For the purposes of this section, *effective exercise premium* means the amount, expressed as a percentage of the warrant's exercise value, by which the sum of the price at issuance and the exercise price of a warrant exceeds its exercise value.

(b) *Sales By Persons Other Than Issuers or Dealers.* Any person, other than the issuer or a dealer, who offers or sells securities in compliance with the conditions set forth in paragraph (d) of this section shall be deemed not to be engaged in a distribution of such securities and therefore not to be an underwriter of such securities within the meaning of sections 2(a)(11) and 4(a)(1) of the Act.

(c) *Sales By Dealers.* Any dealer who offers or sells securities in compliance with the conditions set forth in paragraph (d) of this section shall be deemed not to be a participant in a distribution of such securities within the meaning of section 4(a)(3)(C) of the Act and not to be an underwriter of such securities within the meaning of section 2(a)(11) of the Act, and such securities shall be deemed not to have been offered to the public within the meaning of section 4(a)(3)(A) of the Act.

(d) *Conditions to Be Met.* To qualify for exemption under this section, an offer or sale must meet the following conditions:

(1) The securities are sold only to a qualified institutional buyer or to a purchaser that the seller and any person acting on behalf of the seller reasonably believe is a qualified institutional buyer. In determining whether a prospective purchaser is a qualified institutional buyer, the seller and any person acting on its behalf shall be entitled to rely upon the following non-exclusive methods of establishing the prospective purchaser's ownership and discretionary investments of securities:

(i) The prospective purchaser's most recent publicly available financial statements, *provided* that such statements present the information as of a date within 16 months preceding the date of sale of securities under this section in the case of a U.S. purchaser and within 18 months preceding such date of sale for a foreign purchaser;

(ii) The most recent publicly available information appearing in documents filed by the prospective purchaser with the Commission or another United States federal, state, or local governmental agency or self-regulatory organization, or with a foreign governmental agency or self-regulatory organization, *provided* that any such information is as of a date within 16 months preceding the date of sale of securities under this section in the case of a U.S. purchaser and within 18 months preceding such date of sale for a foreign purchaser;

(iii) The most recent publicly available information appearing in a recognized securities manual, *provided* that such information is as of a date within 16 months preceding the date of sale of securities under this section in the case of a U.S. purchaser and within 18 months preceding such date of sale for a foreign purchaser; or

(iv) A certification by the chief financial officer, a person fulfilling an equivalent function, or other executive officer of the purchaser, specifying the amount of securities owned and invested on a discretionary basis by the purchaser as of a specific date on or since the close of the purchaser's most recent fiscal year, or, in the case of a purchaser that is a member of a family of investment companies, a certification by an executive officer of the investment adviser specifying the amount of securities owned by the family of investment companies as of a specific date on or since the close of the purchaser's most recent fiscal year;

(2) The seller and any person acting on its behalf takes reasonable steps to ensure that the purchaser is aware that the seller may rely on the exemption from the provisions of Section 5 of the Act provided by this section;

(3) The securities offered or sold:

(i) Were not, when issued, of the same class as securities listed on a national securities exchange registered under Section 6 of the Exchange Act or quoted in a U.S. automated inter-dealer quotation system; *Provided,* That securities that are convertible or exchangeable into securities so listed or quoted at the time of issuance and that had an effective conversion premium of less than 10 percent, shall be treated as securities of the class into which they are convertible or exchangeable; and that warrants that may be exercised for securities so listed or quoted at the time of issuance, for a period of less than three years from the date of issuance, or that had an effective exercise premium of less than 10 percent, shall be treated as securities of the class to be issued upon exercise; and *Provided further*, That the Commission may from time to time, taking into account then-existing market practices, designate additional securities and classes of securities that will not be deemed of the same class as securities listed on a national securities exchange or quoted in a U.S. automated inter-dealer quotation system; and

(ii) Are not securities of an open-end investment company, unit investment trust or face-amount certificate company that is or is required to be registered under Section 8 of the Investment Company Act; and

(4)(i) In the case of securities of an issuer that is neither subject to Section 13 or 15(d) of the Exchange Act, nor exempt from reporting pursuant to Rule 12g3-2(b) under the Exchange Act, nor a foreign government as defined in Rule 405 (§ 230.405 of this chapter) eligible to register securities under Schedule B of the Act, the holder and a prospective purchaser designated by the holder have the right to obtain from the issuer, upon request of the holder, and the prospective purchaser has received from the issuer, the seller, or a person acting on either of their behalf, at or prior to the time of sale, upon such prospective purchaser's request to the holder or the issuer, the following information (which shall be reasonably current in relation to the date of resale under this section): a very brief statement of the nature of the business of the issuer and the products and services it offers; and the issuer's most recent balance sheet and profit and loss and retained earnings statements, and similar financial statements for such part of the two preceding fiscal years as the issuer has been in operation (the financial statements should be audited to the extent reasonably available).

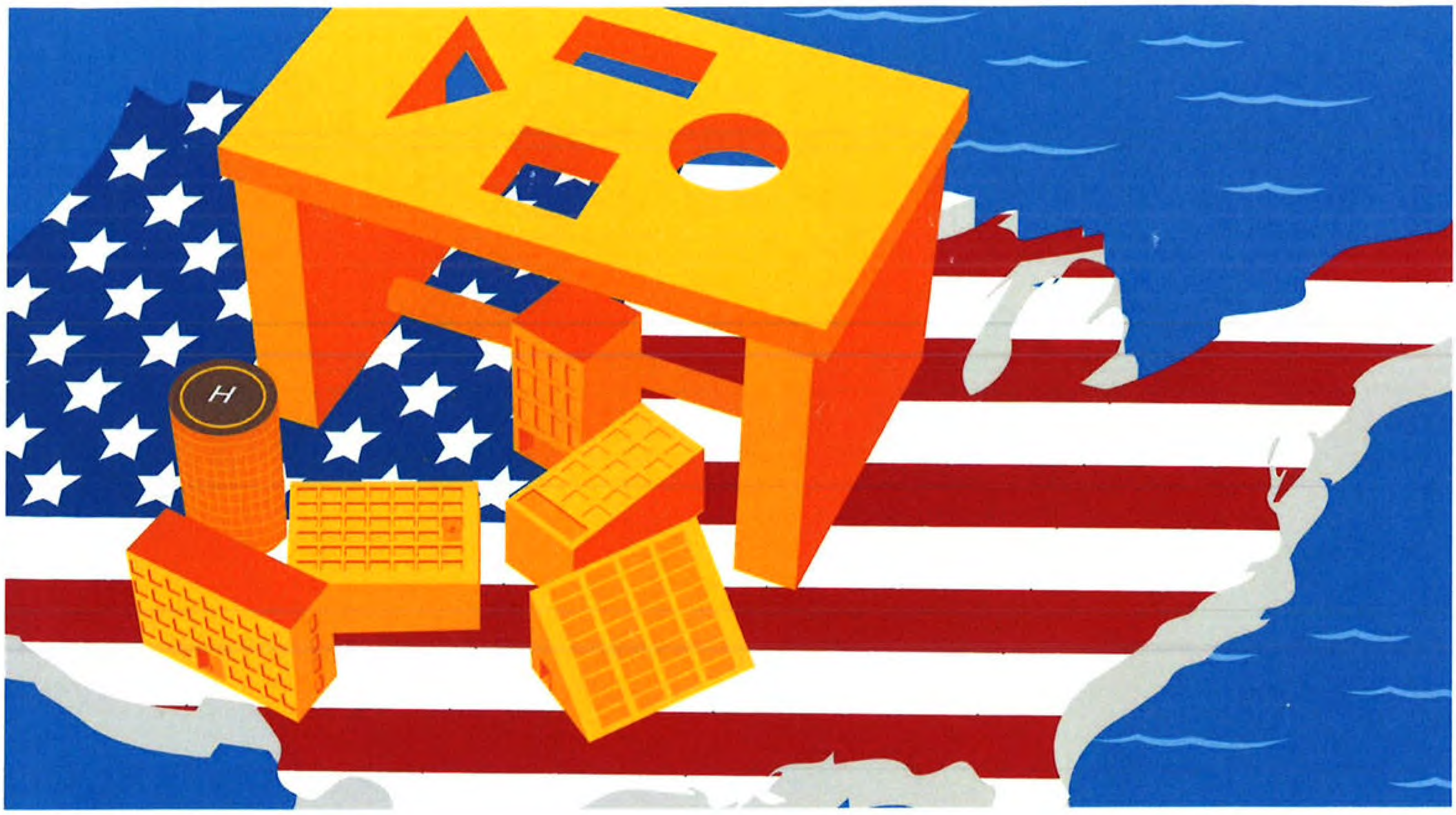
(ii) The requirement that the information be "reasonably current" will be presumed to be satisfied if:

(A) The balance sheet is as of a date less than 16 months before the date of resale, the statements of profit and loss and retained earnings are for the 12 months preceding the date of such balance sheet, and if such balance sheet is not as of a date less than six months before the date of resale, it shall be accompanied by additional statements of profit and loss and retained earnings for the period from the date of such balance sheet to a date less than six months before the date of resale; and

(B) The statement of the nature of the issuer's business and its products and services offered is as of a date within 12 months prior to the date of resale; or

(C) With regard to foreign private issuers, the required information meets the timing requirements of the issuer's home country or principal trading markets.

(e) Offers and sales of securities pursuant to this section shall be deemed not to affect the availability of any exemption or safe harbor relating to any previous or subsequent offer or sale of such securities by the issuer or any prior or subsequent holder thereof.



US PRIVATE PLACEMENTS
WHEN RULE 144A IS UNAVAILABLE

Peter Castellon of Proskauer Rose (UK) LLP and Sebastian Sperber of Cleary Gottlieb Steen & Hamilton LLP examine a private placement exemption from US securities registration requirements that is available to non-US issuers that are offering shares to US investors.

As a general principle of US securities law, all offerings of securities must be registered with the US Securities and Exchange Commission (SEC) or structured to satisfy an exemption from the registration requirements of the US Securities Act of 1933, as amended (Securities Act). Most offerings by non-US companies are structured under exemptions (*see box "Exemptions"*).

Typically, the portion of the offering that takes place outside the US is structured under Regulation S of the Securities Act (Regulation S), and another exemption is used to structure the US portion.

While Rule 144A of the Securities Act (Rule 144A) is the most common exemption used for the US portion in these types of offerings, it is not always available.

Section 4(a)(2) to QIBs is another exemptive route to consider for the US portion. As under Rule 144A, the US portion of the offering is limited to qualified institutional buyers (QIBs) and, as discussed further in this article, there are other similarities to Rule 144A. "Section 4(a)(2) to QIBs" does not exist as a separate statutory exemption, but a practice has developed under which securities of non-US companies are sold to QIBs under Section 4(a)(2) of the Securities Act (Section 4(a)(2)) without imposing some of the procedural restrictions that are used in many US domestic Section 4(a)(2) transactions (*see box "The Section 4(a)(2) exemption"*).

This article focuses primarily on sales to QIBs by the issuer. If Rule 144A is unavailable but the transaction is still structured as a resale to QIBs by a manager, the resale by the manager is, in fact, commonly referred to as a "Section 4(1½)" transaction. Section 4(1½) of the Securities Act (Section 4(1½)) is the interpretive doctrine applicable to resales from one buyer in a private offering to another. As a technical matter, a resale by a financial intermediary in this context is made under Section 4(a)(3), since the financial intermediary is a dealer not acting in the capacity of an underwriter, or participating in a distribution within the meaning of the Securities Act. The private nature of the transaction avoids it being deemed a distribution. Nevertheless, the procedures for conducting Section 4(1½) transactions will be comparable in many instances, especially where the issuer is not listed in the US, to those applicable to direct sales to QIBs by the issuer under Section 4(a)(2) in the contexts described in this article.

This article examines the main uses of Section 4(a)(2) to QIBs for non-US companies. The approach to Section 4(a)(2) outlined in this article is only for transactions directed in the US to QIBs (typically in connection with a concurrent offering outside the US under Regulation S). There are four common transaction scenarios when Section 4(a)(2) to QIBs may be used:

- In equity offerings, as an alternative to Rule 144A when Rule 144A is not considered to be available.
- In equity or debt offerings, where the managers are not obtaining a disclosure letter under Rule 10b-5 of the US Securities Exchange Act of 1934 (Rule 10b-5).
- In rights offerings by non-US companies.
- In mergers and acquisitions (M&A) where local law allows for differential treatment of target shareholders.

In all cases, securities sold under Section 4(a)(2) are restricted. For one year (or, in limited circumstances where the issuer is an SEC reporting company, for six months), the securities can only be sold in the US to other QIBs or in other private transactions; however, the securities can be sold outside the US at any time under Regulation S.

Exemptions

Non-US issuers may be able to rely on the following exemptions from the registration requirements of US securities laws:

- The US Securities and Exchange Commission's Regulation D provides issuers with a safe harbour from the registration requirements of the US Securities Act of 1933 (Securities Act). Rule 506 of Regulation D allows issuers to sell their securities in a private placement to an unlimited number of accredited investors, provided that issuers comply with the general requirements of Regulation D.
- Section 4(a)(2) of the Securities Act (*see box "The Section 4(a)(2) exemption"*).
- Rule 144A under the Securities Act provides an exemption from the registration requirements for resales of securities to certain institutional buyers.
- Regulation S under the Securities Act provides a safe harbour from the registration requirements of the Securities Act for offers and sales of securities outside the US where certain conditions are fulfilled.

ALTERNATIVE TO RULE 144A

Section 4(a)(2) can be used for primary offerings of equity securities to QIBs when Rule 144A is not available. Rule 144A could be unavailable because the securities were fungible, when issued, with securities listed on a US exchange, which is a condition of relying on the rule (*Rule 144A(d)(3)*). In the context of secondary offerings of equity securities to QIBs where the issuer of the securities is not involved, Rule 144A could be unavailable because the information furnishing requirement of Rule 144A is not satisfied.

Another common scenario is where Rule 144A is not considered to be available because the intermediaries are not buying and reselling the securities. Rule 144A, by its terms, is an exemption for resales. In order to comply with the exemption, either the seller must be a shareholder (although a subsidiary company would not be eligible to rely on Rule 144A) or, in a primary offering where the seller is the issuer, the manager must buy the shares and resell them to investors.

In some non-US jurisdictions, primary offerings are structured in such a way that the financial intermediary does not buy and resell. This can be driven by local tax or corporate law concerns, or it may be local market practice. The UK is one jurisdiction where the local practice is for agreements in London-listed initial public offerings (and other securities offerings) to be structured in such a way that the managers do not buy and resell.

Some market participants address in another way the absence of a resale of all the shares being offered. If the offering is not a resale by underwriters but is an offering of a mix of secondary and primary shares, and there is a sufficient number of secondary shares to cover US demand and the secondary shares can be segregated from the primary shares, the offering is sometimes structured under Rule 144A by selling only secondary shares to QIBs. In this way, a shareholder, and not the underwriter, is technically reselling the shares to the QIBs. Limiting US sales to secondary shares, however, means that US liability risks might be disproportionately borne by the selling shareholder. If there are not enough secondary shares or the secondary shares cannot be segregated, or if the offering is of primary shares only, the US portion of the offering can be structured under Section 4(a)(2) to QIBs. If the offering is of secondary shares only, the offering can be conducted under Rule 144A.

Procedures

The procedures for Section 4(a)(2) to QIBs transactions can be very similar to those for a Rule 144A transaction, except for the absence of a resale of the securities:

- Offers and sales are made in the US to QIBs only.
- The same offering document that would otherwise be used for a Rule 144A offering is used. US securities law legends at the front of the document, but not the transfer restrictions, might differ slightly.
- The financial intermediaries receive the same Rule 10b-5 disclosure letters and SAS 72 comfort letters (*see boxes "Rule 10b-5 disclosure letter" and "SAS 72 comfort letter"*).
- The issuer provides the same representations and covenants in the placing or underwriting agreement, including the ongoing information covenant that relates to information required by Rule 144A(d)(4). By comparison, in a Section 4(1½) transaction, where there is a selling shareholder, the seller provides the same representations and covenants in the placing or underwriting agreement, other than the ongoing information covenant.

- QIBs do not sign investor representation letters, except where the securities being offered and sold are fungible with securities listed on a US exchange, in which case investor representation letters and other procedures would need to be considered.

In the UK, primary equity offerings by companies listing on the London Stock Exchange (and other offerings of equity securities) are usually structured as a direct primary sale from the issuer to the ultimate investor. Under the typical UK structure, the manager will only buy the shares if an investor defaults between the time the underwriting agreement is signed and the closing of the offering. Because Rule 144A is an exemption for resales, some argue that Rule 144A is not available and that Section 4(a)(2) to QIBs is the appropriate exemption for the manager's activities. A number of market participants take a different view.

In the UK structure, as in a traditional Rule 144A offering, the investment banks serve as intermediaries that bear the ultimate economic risk of the offering not being fully subscribed through a standby arrangement with the issuer. This so-called "Rule 144A direct" offering structure thus has no impact on economics, which are identical to the traditional Rule 144A offering. By contrast, in a classic Section 4(a)(2) offering, the issuer bears the economic risk if the placement agent (if any) does not find investors. Because the investment banks soliciting prospective investors bear the economic risk rather than the issuer in these offerings and are functionally indistinguishable from the intermediaries in a traditional Rule 144A offering, the applicable Section 5 exemption for their offering activities is interpreted by some market participants to be Rule 144A. Section 4(a)(2) is the exemption for the direct issuer sales to investors under this analysis even if Rule 144A is the exemption applicable to the manager's offering activities.

The Section 4(a)(2) exemption

Section 4(a)(2) is an exemption from the registration requirements of the US Securities Act of 1933 (Securities Act), for "transactions by an issuer not involving any public offering." In the domestic practice in the US, an issuer often approaches a small number of institutional investors and the investors subscribe to securities of the issuer. The investors typically sign a subscription agreement with the issuer and carry out their own due diligence.

Although there will often be a financial intermediary acting as a placement agent in Section 4(a)(2) transactions, the financial intermediary does not underwrite the securities, and may not even pass the securities through its books; this might be the case, for example, if the issuer is handling the sale itself in reliance on the Rule 3a4-1 safe harbour from the broker-dealer registration requirements under the US Securities Exchange Act of 1934, as amended, which may be available for certain securities offerings.

In domestic US Section 4(a)(2) transactions, companies often approach both qualified institutional buyers (QIBs) and accredited investors. While it is possible to offer and sell securities to non-QIB institutional investors in the US under Section 4(a)(2), those transactions typically involve different procedures. It is also possible (although rare) to use Section 4(a)(2) (without resort to certain safe harbours under Section 4(a)(2)) to sell to a limited number of individuals in the US. Again, different procedures are used in those transactions.

NO RULE 10B-5 DISCLOSURE LETTER

In a typical offering of securities of a non-US company that is extended into the US, the underwriters will receive Rule 10b-5 disclosure letters, and the offering will be structured under Rule 144A or, in some cases, will be registered with the SEC. Investment banks take different approaches to whether to extend offerings of securities of non-US companies in the US in the absence of a Rule 10b-5 disclosure letter. Some banks will not do it at all, while others will only do it for offerings of debt securities. Of those that sometimes extend equity offerings to the US in this circumstance, some only do it in a limited manner for rights offerings (*see "Rights offerings by non-US companies" below*).

For those investment banks prepared to do so other than for rights offerings, one of two scenarios often apply:

- The offering was originally structured under Regulation S but, late in the process, the US is included; for example, as a result of a reverse inquiry from a potential investor in the US.

- The US portion of the offering is so small that, from a risk perspective, the managers are comfortable including the US without the more typical comfort of a Rule 10b-5 disclosure letter or, in many cases, a SAS 72 comfort letter.

A Section 4(a)(2) placement to QIBs is often the offering structure chosen in these scenarios. The managers take steps to support the argument that investors are not relying on them in making their investment decisions. Reliance is a requirement in a private Rule 10b-5 action (but not in an action by the SEC). Managers typically approach only a limited number of QIBs in these circumstances, and they ask the QIBs to sign investor representation letters. While there is no numerical limit, only a small number of QIBs that are known to the manager, or are known to the issuer or selling shareholder, are typically approached in the US in these circumstances.

The investor representation letter normally contains the following representations:

- The investor is satisfied with the level of information that it has received and is not relying on any investigation by, or representation from, the managers.

- The investor is a QIB.

- The investor understands that the securities are restricted.

Sometimes there are longer letters that contain so-called big boy or toxic language. These letters contain provisions in which the investor acknowledges certain risks of the securities or of the issuer, and the limited involvement of the placement agent. There are differing views on the effectiveness of toxic language.

Rule 10b-5 disclosure letter

Rule 10b-5 under the US Securities Exchange Act of 1934 (Rule 10b-5) provides that liability in connection with an offering document may arise if material information is omitted or materially misleading information is included. A Rule 10b-5 disclosure letter is a letter from lawyers confirming that, having undertaken certain due diligence procedures, they have no reason to believe that an offering document contains an untrue statement of material fact or omits to state a material fact necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading.

The managers often act as agents in connection with the US portion of the offering and do not buy and resell the securities. The securities are placed directly by the issuer with investors.

Because the portion of the offering structured in this way under Section 4(a)(2) to QIBs is usually part of a larger offering, it is not usually possible to reflect the more customary features of a domestic Section 4(a)(2) placement. For example, there would not likely be a separate subscription agreement between the issuer and the investor, or direct negotiations of the terms of the trade with the issuer. This structure can be used for both equity and debt securities.

RIGHTS OFFERINGS BY NON-US COMPANIES

When a non-US company extends its rights offering into the US, it must register the rights offering with the SEC or structure the rights offering to comply with exemptions from the registration requirements of the Securities Act. There are three potential stages of a rights offering where exemptions need to be considered.

- Distribution of the rights to US shareholders. This is typically done without consideration, so it should not be treated as an offer or sale that needs to be registered with the SEC.

- Exercise of the rights by US shareholders or other US rights holders. There are several exemptions that will potentially be available. Rule 801 under the Securities Act, which is applicable if 10% or less of the shares are held of record by US holders, is sometimes, but rarely, used. Section 4(a)(2) to QIBs is an available exemption. Rule 144A frequently is not available for the exercise because it is not intermediated. (Regulation S is available for non-US shareholders and other non-US rights holders.)

- Placement of the rump. The portion of a rights offering not taken up by rights holders can be placed under a number of exemptions (and the rights offering may, or may not, be underwritten). Regulation S can be used if the managers exclude the US. If the managers include the US, the most common exemptions are Rule 144A and Section 4(1½). If the managers are placing the rump shares without buying and selling them, for example, in a non-underwritten rights offering, Section 4(a)(2) to QIBs is available. Section 4(a)(2) will not be available where the managers have underwritten and are buying and reselling the rump shares.

Disclosure models

There are three disclosure models for rights offerings:

- Those extended into the US with a Rule 10b-5 disclosure letter.

- Those extended into the US without a Rule 10b-5 disclosure letter.

- Those excluding the US.

In a rights offering extended into the US with a Rule 10b-5 disclosure letter, the managers typically are involved in roadshows and in soliciting US shareholders. The offering document is written to a Rule 10b-5 standard. The managers also usually obtain a SAS 72 comfort letter. The exercise of the rights by US shareholders and other US rights holders is frequently structured under Section 4(a)(2) to QIBs, and the rump placement is typically structured under Rule 144A or as a Section 4(1½) to QIBs transaction. This is because the exercise of rights does not involve a resale, but the rump placement usually does.

In a rights offering extended into the US without a Rule 10b-5 disclosure letter, the offering document is typically prepared to a high standard, but not necessarily with the same level of information and degree of involvement by US-qualified attorneys and accountants as would be the case where Rule 10b-5 letters and SAS 72 comfort letters are delivered to the managers. The offering document frequently provides that shareholders in the US are excluded "subject to certain exceptions."

Those exceptions are typically QIBs approached under Section 4(a)(2). Usually, the issuer approaches its US shareholders that are QIBs directly, without involving the managers; the managers nevertheless often help the issuer confirm which of the issuer's US shareholders are QIBs. (Issuers would need to be mindful of considerations under the broker-dealer registration requirements in the US, especially if they approach US shareholders in this manner on a recurring basis.)

US shareholders and other US rights holders that are QIBs will exercise their rights under Section 4(a)(2). Under this model, the rump is typically not placed with

SAS 72 comfort letter

The form and content of the most commonly used comfort letter in international offerings is governed by the US accounting profession's AU Section 634 "Letters for Underwriters and Certain Other Requesting Parties", and is generally referred to as SAS 72 as it was initially issued as Statement on Auditing Standards No 72. SAS 72 contains specific instructions that govern when, and to whom, a comfort letter may be issued, the scope of information that may be provided within a comfort letter, as well as examples of comfort letters that should be delivered in certain situations (*see feature article "SAS 72 letters: seeking comfort", www.practicallaw.com/1-525-4623*).

US investors because of liability concerns for the managers given the absence of a Rule 10b-5 disclosure letter.

In a rights offering excluding the US, US shareholders are not able to exercise their rights, and the rump is placed outside the US. The rights, if transferable, or new shares attributable to the excluded US shareholders, are often sold in the open market outside the US, with the net proceeds remitted to the US shareholders.

M&A TRANSACTIONS

M&A transactions that involve an exchange of a bidder's securities for those of the target, as opposed to cash-only transactions, also implicate the registration requirements of the Securities Act. Some transactions might be able to benefit from exemptions from the registration requirements not generally applicable in other contexts, such as Section 3(a)(10) of the Securities Act (which could apply to a scheme of arrangement) or Rule 802 under the Securities Act (applicable if 10% or less of the shares of the target are held of record by US shareholders).

If the applicable non-US corporate law in a transaction allows differential treatment of certain holders of target securities, it also might be possible to use Section 4(a)(2) to exchange bidder securities for target securities held by certain US target shareholders (such as QIBs) without registering the transaction with the SEC. This could involve offering bidder shares only to those target shareholders that can certify that they are QIBs and applying procedures similar to those outlined above to satisfy the requirements of Section 4(a)(2).

The offering materials might provide, for example, that shareholders of the target in the US are excluded "subject to certain exceptions". Those exceptions are the QIBs approached under Section 4(a)(2). Section 4(a)(2) can be used in situations where Rule 802 is not available or where it is not practical to determine if it is available. The structure might not be appropriate if there is a large number of US retail shareholders. Such an approach would not be possible where the target's equity is listed in the US and the transaction is being structured as an exchange offer.

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THE RULES OF RULE 144A

Proskauer's Peter Castellon discusses how to comply with the continuing information requirements of Rule 144A.

Rule 144A is an exemption for sales of securities in the United States to a type of institutional investor known as a Qualified Institutional Buyer or QIB. To comply with the rule, several requirements must be met:

- The securities may only be sold to QIBs or purchasers that the seller and any person acting on behalf of the seller reasonably believe to be QIBs (Rule 144A(d)(1)).
- The seller and any person acting on its behalf must take reasonable steps to ensure that the purchasers are aware that that the seller may rely on Rule 144A (Rule 144A(d)(2)).
- The securities must ***not*** have been, ***when issued***, of the same class as shares listed on an exchange in the United States (Rule 144A(d)(3)(i)).
- The issuer may ***not*** be of an open-ended investment company, unit investment trust or face-amount-certificate company that is, or is required to be, registered under the U.S. Investment Company Act of 1940, as amended (Rule 144A(d)(3)(ii)).
- The issuer must be a reporting company under the U.S. Securities Exchange Act of 1934, as amended, ***or*** regularly furnish information to the SEC ***or*** agree to provide certain information to holders of its securities upon request for themselves or on behalf of prospective purchasers (Rule 144A(d)(4)(i)).

In addition, there was a prohibition on general solicitation. The SEC lifted the prohibition in response to the Jobs Act. In practice, many underwriting or placing agreements in Rule 144A transactions continue to prohibit general solicitation.

If the securities do not meet the eligibility requirements of paragraph (d)(3) ***or*** if the issuer is unwilling or unable to comply with the requirements of paragraph (d)(4), an offering will frequently be structured pursuant to an interpretation of the Securities Act commonly known as Section 4(1½).

Ongoing information requirements

This article focuses on the fifth of these requirements: paragraph (d)(4) of Rule 144A regarding ongoing information. There are several ways to meet the ongoing information requirements:

First, the requirements are met if the issuer has securities listed on an exchange in the United States or otherwise has securities registered with the Commission. The securities listed on an exchange in the United States need ***not*** be those that are sold in the Rule 144A offering. For example, an issuer offering debt securities will meet the requirements if it has American depositary receipts listed on the New York Stock Exchange.

Second, the requirements are met if the issuer complies with Rule 12g3-2(b).

Third, the requirements are met for debt securities if the issuer is a non-U.S. government or political subdivision of a non-U.S. government.

Fourth, the requirements are met if holders of the securities offered, and prospective purchasers designated by holders, have the right to obtain from the issuer certain specified information. Investors must have the right to obtain the specified information from the issuer. The requirement is ***not*** met by an undertaking from a selling shareholder to provide the information.

How to comply

The most common method of satisfying the ongoing information requirement is the fourth: obtaining a covenant from the issuer to provide the information. If the issuer is a reporting company (that is, it has securities listed on an exchange in the United States or is registered with the Commission and files regular reports with the Commission) or is Rule 12g3-2(b)-compliant, then a covenant is not needed. Few European issuers are reporting companies and few are known to be Rule 12g3-2(b)-compliant, so the default is the fourth method.

Similarly, the covenant is not needed if the issuer is exempt from reporting pursuant to Rule 12g3-2(b). This rule is an exemption from the reporting requirements of Sections 13 and 15(d) of the Exchange Act for non-U.S. companies that make certain information publicly available. As explained in 'U.S. style home country disclosure', it is sometimes not easy or not possible to confirm whether the issuer is Rule 12g3-2(b)-compliant. This is sometimes the case in block trades and other secondary transactions, where the issuer might not be aware of the transaction. In the case of a primary offering, it should always be possible to establish whether an issuer is Rule 12g3-2(b)-compliant.

If the issuer or selling shareholder is able to represent that the issuer is Rule 12g3-2(b)-compliant, or the law firms or banks involved are able to establish compliance based on an examination of the issuers' publicly available information, then this method should be used to meet the requirements of paragraph (d)(4).

If the issuer is not a reporting company, not exempt from reporting pursuant to Rule 12g3-2(b) (or if 12g3-2(b) compliance cannot be confirmed or established), and not a non-U.S. government issuing debt, there is a different way to comply with paragraph (d)(4). The issuer must give the holders of the securities (and prospective purchasers designated by the holders) the right to obtain information from the issuer.

In primary offerings, this is most often accomplished through a covenant in the underwriting or placing agreement. In the case of New York law-governed agreements, the holders will have third-party rights under the agreement. In the case of an English law-governed agreement where there is an exclusion of third-party rights, the covenant is often carved-out of the exclusion.

If the issuer is not a party to the agreement, the right can be granted to holders (and their designees) through an English law deed poll.

The information that holders and their designees must have a right to obtain from the issuer is the following:

- a very brief statement of the nature of the business of the issuer and the products and services it offers

- the issuer's most recent balance sheet and profit and loss and retained earnings statements

- similar financial statements for such part of the two preceding fiscal years as the issuer has been in operation.

The financial statements should be audited to the extent reasonably available. For European issuers, the required information must meet the timing requirements of the issuer's home country or principal trading market. The ongoing information requirements can typically be met by sending the shareholder (or its designee) a copy of issuer's most recent annual report.

If the issuer is unable or unwilling to agree to provide the ongoing information, the most common approach is to structure the offering pursuant to Section 4(1½), rather than Rule 144A.

The question sometimes arises whether another approach can be used. The adopting release for Rule 144A, which was promulgated in 1990, contains the following passage:

> *The Rule does not specify the means by which the right to obtain information would arise. The obligation could be, inter alia, imposed in the terms of the security, by contract, by corporate law, by regulatory law, or by rules of applicable self-regulatory organizations.*

Based on the passage, some lawyers question whether the requirements of paragraph (d)(4) will be met if the laws of issuer's jurisdiction of incorporation, or regulations of the issuer's exchange, require the issuer to make public the information required by Rule 144A. For European issuers, this will almost always be the case. European annual reports always contain more information than is required by the rule.

This is an updated version of an article that originally appeared in the January, 2013 edition of IFLR.

Rule 135e legend

Rule 135e provides a safe harbor for announcements, press releases and other press-related materials in connection with an offering structured pursuant to Regulation S. Inserting the legends below will have the effect of the press release ***not*** constituting general solicitation, general advertising or directed selling efforts.

The following legend should be inserted at the top of the press release in all-capital letters:

> NOT FOR RELEASE, PUBLICATION OR DISTRIBUTION IN WHOLE OR IN PART IN OR INTO THE UNITED STATES, CANADA OR JAPAN.

The following legend should be inserted at the end of the press release in addition to any legends or rubrics that might be required by local law or practice:

> This announcement is not for publication or distribution, directly or indirectly, in or into the United States of America. This announcement is not an offer of securities for sale into the United States. The securities referred to herein have not been and will not be registered under the U.S. Securities Act of 1933, as amended, and may not be offered or sold in the United States, except pursuant to an applicable exemption from registration. No public offering of securities is being made in the United States.

The first legend should always include Canada, ***unless*** a Canadian lawyer has been consulted. There is a practice developing of including further jurisdictions, such as Australia, South Africa and New Zealand. There is ***no*** need to include New Zealand. There is also practice of including a sweep-up clause (such as "and any other jurisdiction where such activity would be unlawful"). You should ***not*** use a sweep-up clause: it is of ***no*** help to the person distributing the press release.

The second legend should be inserted in announcements or press releases as its own, stand-alone paragraph. It should ***not*** be combined with other legends.

In the case of an advertisement in a non-U.S. publication, such as the Financial Times, the first legend can be omitted.