

SEC Proposes Expansion of “Test-the-Waters” Communications to All Issuers

On February 19, 2019, the Securities and Exchange Commission (SEC) proposed a rule that would expand the “test-the-waters” accommodation — currently available only to emerging growth companies (EGCs) — to all issuers. If adopted, the new Rule 163B would enable all issuers, or any person authorized to act on their behalf, including underwriters, to make oral and written offers to qualified institutional buyers (QIBs) and institutional accredited investors (IAIs) prior to or after the filing of a registration statement to gauge market interest in a possible initial public offering or other proposed registered securities offerings.

The rule was proposed in response to recent calls for the SEC to expand the testing-the-waters accommodation beyond EGCs to all issuers and is intended to facilitate registered offerings by providing increased flexibility with respect to communications with institutional investors. The SEC’s proposal follows action taken by the Division of Corporation Finance in 2017 to extend another EGC accommodation — the ability to initially submit certain filings on a confidential basis — to all issuers.

Background

In 2012, Congress passed the Jumpstart Our Business Startups Act (JOBS Act), which permits an EGC and any person acting on its behalf to engage in oral or written communications with potential investors that are QIBs or IAIs before or after filing a registration statement in order to assess investor interest in a contemplated securities offering. Permitting EGCs to test-the-waters was intended to ease long-standing restrictions on “gun-jumping” under Section 5 of the Securities Act of 1933, as amended (the Securities Act), in order to provide increased flexibility to EGCs with respect to such communications, as well as to serve as a cost-effective means for evaluating market interest before incurring the costs associated with such an offering.

Proposed Rule

Proposed Rule 163B would permit any issuer (including a non-reporting issuer), or any person authorized to act on its behalf, to engage in oral or written communications with potential investors that are, or are reasonably believed to be, QIBs or IAIs, either prior to or following the filing of a registration statement. The testing-the-waters rule and the related proposal are intended to help issuers assess the demand for and valuation of their securities, which in turn could improve the ability of issuers to conduct successful offerings and lower their cost of capital, thereby encouraging additional participation in the public markets.

While exempt from restrictions imposed by Section 5 of the Securities Act on written and oral offers prior to or after filing a registration statement, these communications would nonetheless still be considered “offers” as defined in Section 2(a)(3) of the Securities Act and would therefore be subject to Section 12(a)(2) liability in addition to the anti-fraud provisions of the federal securities laws. The proposed rule would be non-exclusive; attempted compliance would not act as an exclusive election and an issuer could rely on other Securities Act communications rules or exemptions when determining how, when and what to communicate related to a contemplated securities offering.

While the communications would not need to be filed with the SEC (and would be excluded from the definition of free writing prospectus), the SEC could request that an issuer furnish it with any test-the-waters communication used in connection with an offering. Issuers subject to Regulation FD would also need to consider whether any information in a test-the-waters communication could trigger disclosure obligations under Regulation FD. To avoid the application of Regulation FD, the



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proposing release notes that an issuer could consider obtaining confidentiality agreements from any potential investor engaged under the proposed rule.

Request for Comment

The proposal will be subject to a 60-day public comment period following publication in the Federal Register.

The proposed rule can be found [here](#).
