FENWICK & WEST LLP

Corporate and Securities Law Update

Sweeping New Rules Apply to Securities Offerings by Technology and Life Science Companies

SEPTEMBER 30, 2005

A MAJOR MODERNIZATION OF FEDERAL REGULATIONS THAT APPLY TO REGISTERED SECURITIES OFFERINGS TAKES EFFECT DECEMBER 1, 2005. The changes include welcome improvements to current rules, as well as new concepts that may, over time, fundamentally alter how some registered offerings are conducted. This update introduces the aspects of the new rules that are most salient to high technology and life sciences companies.

Securities offering reform clusters around three principal topics:

- Loosening restrictions on communications in connection with registered securities offerings.
- Streamlining the Securities Act registration process, particularly for shelf registrations.
- Rationalizing liability issues, particularly relating to timing of Securities Act liability.

New concepts, notably "free writing prospectus" and "well-known seasoned issuer," are entering the securities regulation lexicon as part of the new rules. Those terms are defined in the attached glossary, but the general concepts are as follows:

- A free writing prospectus is a written offer, other than the required statutory preliminary or final prospectus, that is not otherwise exempt from the broad definition of offer.
- A well-known seasoned issuer is a large issuer (e.g., at least $700 million of unaffiliated market capitalization) that is eligible to use Form S-3 registration statements for primary offerings and is not an ineligible issuer, as defined in the rule.

For the sake of simplicity, this update does not address topics related to foreign private issuers and asset-backed issuers.

This update provides only an overview of these new rules; we encourage you to contact members of your Fenwick & West team to discuss any questions you may have about how the rules apply to your specific situation. For your further reference, the complete text of the SEC's adopting release is available at this link: http://www.sec.gov/rules/final/33-8591.pdf.

INTRODUCTION

What led the SEC to reform the securities offering rules?

For many years, the SEC has recognized the need to modernize federal regulation of securities offerings. The underlying laws, adopted in 1933 and 1934, have been amended many times, and over the years the SEC has promulgated a large body of rules and regulations, supplemented by a complex set of formal and informal interpretive advice and practice. Some of the new rules simply codify existing informal advice and practice.

A major impetus for securities reform has been the advances in technology that have dramatically increased the amount of information available about public companies, and the speed at which information is disseminated. In addition, the reliability of public company periodic reports has increased in response to greater regulation—some of which grew out of the Sarbanes-Oxley Act of 2002—requiring more, faster, better disclosure.

Understanding the regulatory tension between corporate communications with the investment community that are ongoing, frequent and clear, on the one hand, and a regulatory framework designed to limit those communications, on the other, in this reform the SEC came down in favor of the ongoing communications. The new rules focus less on whether an offer is legal or illegal, and more on whether it was an honest, accurate offer.

When are the new rules effective?

December 1, 2005 is the effective date of the new rules. The SEC Division of Corporation Finance has also published guidance to cover transitional situations, such as shelf registration statements that are already on file. The staff FAQ on these transitional issues is available at this link: http://www.sec.gov/divisions/corpfin/transitionfaq.htm.

How do the new rules affect my company?

The new rules primarily relate to securities offerings, so they will apply, for example, when your company raises capital through a registered offering of common stock. The SEC has also made some changes to periodic report filings, such as requiring that a company's annual report on Form 10-K include a section discussing material risk factors.

I have heard that the new rules designate some issuers as "well-known seasoned issuers." Why? What other categories of issuer are there?

One of the most significant innovations of the new rules is the concept of "well-known seasoned issuers." The SEC has given these companies the greatest degree of flexibility in the conduct of securities offerings. Generally, these are companies that are eligible to use Form S-3 for primary offerings, are current and timely in their Exchange Act filings, have a market capitalization in excess of $700 million, and are not an ineligible issuer as defined in the rule. For a more complete definition, see the glossary. These companies, their SEC filings and their many informal disclosures are closely followed by the financial press and professional securities analysts, with whom the companies are in regular dialogue, so the market is best informed about these public companies. Representing about 30% of all listed issuers, well-known seasoned issuers account for about 95% of U.S. equity market capitalization.

Other issuers are "seasoned issuers" (companies that are eligible to use Form S-3 for primary offerings), "unseasoned issuers" (required to file reports under the Exchange Act but not eligible to use Form S-3), "reporting issuers" (any company required to file Exchange Act reports), and "non-reporting issuers" (not required to file Exchange Act reports; includes companies conducting an IPO).

In order to understand how the securities offering reform rules affect your company, it is important that you first determine the category of issuers to which your company belongs.

COMMUNICATIONS RULES

What is the basic regulatory framework governing communications around securities offerings before the new rules go into effect?

Today, all companies involved in registered securities offerings are subject to the same regulatory framework, under which the determination of what communications are permitted depends on the stage of the company's offering. These are generally referred to as the "gun-jumping" provisions of the securities regulations. Violating the gun-jumping rules can result in an illegal offer of securities.

During the "pre-filing period"—before a registration statement is on file—the Securities Act prohibits all offers to sell securities and all solicitations of offers to buy securities. During the "pre-effective" period—after filing and before the SEC declares the registration statement effective—all types of oral offers are permitted, but written offers must conform to specific information requirements (typically, a "red herring" prospectus). In the "post-effective period"—after the registration statement is effective—oral offers are still permitted and supplementary written materials can be used if accompanied or preceded by a final prospectus.

What is different after December 1, 2005? What are the major areas of change under the new communications rules?

The existing framework of gun-jumping rules was conceived with investor protection in mind, but dramatic changes in communications technology are part of the reason the SEC concluded that investors would benefit from access to more permitted communications. The SEC intends the regulatory focus to be the accuracy of disclosures made to investors at the time of their investment decisions.

The new rules significantly liberalize the ability to communicate with investors in both the pre-filing and pre-effective periods of a registered public offering. The degree of liberalization is different for different categories of issuer

companies, depending upon their reporting histories and their market capitalizations. Notable changes, which are explored in more detail below, include:

- Well-known seasoned issuers may engage at any time in oral and written communications, subject to few conditions, such as legend requirements and filing requirements for free writing prospectuses.
- All reporting issuers may publish regularly released factual business information and forward-looking information, even during the quiet period for an offering.
- Non-reporting issuers may publish regularly released factual business information (but not forward-looking information), for use by non-investors, even during the quiet period.
- Issuer communications more than 30 days before filing a registration statement are permitted so long as they do not refer to the offering, and provided the issuer takes steps within its control to prevent distribution during the 30-day period.
- After filing the registration statement, issuers may use free writing prospectuses—not just formal preliminary prospectuses and prospectus supplements—under certain conditions.
- Issuers are permitted to disclose more information about the company and the offering under existing Rule 134.

In general, how are the communications rules for the pre-filing period different?

Well-known seasoned issuers will now be permitted to make oral or written communications at any time, including during the pre-filing period. Specifically, new Rule 163 completely exempts from Securities Act Section 5(c) all **oral** offers by well-known seasoned issuers in the pre-filing period. It also exempts all **written** offers by well-known seasonal issuers (deeming them to be free writing prospectuses) if they satisfy legend and filing requirements of the rule. Cure provisions are available for immaterial or unintentional failures to include the specified legend or to file the free writing prospectus. This exemption is not available for communication relating to a business combination.

Other issuers (with exceptions noted below) will also be permitted to make oral or written communications in the pre-filing period if they comply with somewhat more significant conditions than those for well-known seasoned issuers. Interviews with the press, investor communications press releases, website material, and all other oral or written communications will be permitted in the pre-filing period. The conditions are: first, that the communication is made more than 30 days before the filing of a registration statement for a securities offering and does not reference the offering; and second, that the company takes reasonable steps to prevent further distribution of that communication during the 30-day period leading up to the registration statement filing. This liberalized rule is not available to an issuer that is (or, including predecessors, in the past three years was) a blank check company, a shell company, or an issuer in an offering of penny stock. The exemption is not available for communications relating to a business combination.

In addition, two new safe harbors are now available for communications in the pre-filing period (including during the 30 days prior to filing the registration statement). Rule 168 permits all reporting issuers (except voluntary filers) to disseminate factual business information and forward-looking information, if they have done so previously. Rule 169 permits non-reporting issuers to disseminate factual business information (but not forward-looking information) to persons other than investors, if they have done so previously. In both cases, the company previously must have publicly disseminated the relevant type of information in the ordinary course of its business, and the timing, manner and form of continued releases must be materially consistent with past practice. Neither safe harbor extends to information about the offering itself. With respect to information outside the safe harbors, companies must assess whether or not any such communication is an offer under the SEC's traditional analysis by evaluating the timing, content and audience of the communication.

How are the communications rules for the pre-effective period different?

Well-known seasoned issuers can continue to make oral or written offers during the pre-effective period.

For other companies, the safe harbors for factual business information and forward-looking information, discussed above, continue to apply during the pre-effective period. In addition:

- More information can now be presented in a Rule 134 notice.
- Issuers are able to use "free writing prospectuses" under certain conditions.
- New rules apply to the conduct of road shows.

How has Rule 134—the existing safe harbor for written disclosures in the pre-effective period—been revised to increase the amount of information that can be disclosed?

Rule 134 provides a safe harbor from the gun-jumping rules for disclosures, during the pre-effective period, of a limited amount of information about an offering. As revised, Rule 134 permits:

- More (but still limited) information about the issuer and its business, including contact information.
- More information about the terms of the offering.
- More information about the offering, such as schedule and procedural information.
- More information about directed share plans and other participation by employees, officers and directors.

What is a "free writing prospectus"?

A free writing prospectus is a written communication (including an electronic communication), used after filing a registration statement, that constitutes an offer to sell or a solicitation of an offer to buy securities in the offering and that is not a statutory preliminary or final prospectus. For a more complete definition, see the glossary.

In an invitation to open up securities offering communications practices, new Rule 164 permits the use of a free writing prospectus between filing and effectiveness of the registration statement—in addition to the traditional preliminary prospectus (a "red herring") or shelf offering prospectus supplements. Offering participants other than the company, such as underwriters, can also prepare and use free writing prospectuses in compliance with the new rules.

Are all issuers eligible to use free writing prospectuses?

No. Free writing prospectuses are not available to "ineligible issuers," which include companies that are not current in their reporting obligations, companies that have violated anti-fraud provisions of the securities laws, and issuers where there may be greater potential for abuse, such as blank check companies, shell companies and penny stock issuers.

When can a well-known seasoned issuer use a free writing prospectus? What about a seasoned issuer? An unseasoned issuer? A non-reporting issuer?

A well-known seasoned issuer can make written offers during the pre-effective period, just as it can during the pre-filing period, subject to the same legend and filing requirements. Those communications are free writing prospectuses.

A seasoned issuer—one that is eligible to use Form S-3 to sell its securities—may use a free writing prospectus after filing a registration statement that contains a statutory prospectus, which may be the base prospectus in a shelf offering. For these issuers (unlike companies conducting an IPO), the "red herring" prospectus need not accompany or precede the free writing, so long as its availability is noted.

An unseasoned issuer—one that is not yet eligible to use Form S-3 to sell its securities—and a non-reporting issuer—such as a company in its initial public offering—may use a free writing prospectus in connection with its offering if (i) a registration statement that contains a statutory prospectus has been filed, and (ii), in most instances, the free writing prospectus is accompanied or preceded by a "red herring" prospectus. Note that delivery of the red herring may be accomplished by hyperlink in an electronic communication, and that the statutory prospectus must contain a bona fide price range for a free writing prospectus to be used.

What information may be contained in a free writing prospectus ?

No specific disclosure requirements govern the contents of a free writing prospectus, except for a legend requirement.

As a result, a free writing prospectus that satisfies the conditions of Rule 433 may include information that is not included in the registration statement for the securities offering. However, the contents of the free writing prospectus may not conflict with the information in the registration statement, and the liability provisions of Securities Act Section 12(a)(2) apply to it. The SEC provided no guidance on what it means for a free writing prospectus to conflict with the information in the registration statement. However, if an issuer determines that such a conflict does exist, it can resolve the conflict by filing the free writing prospectus with a Form 8-K that is incorporated into the registration statement.

The SEC staff may request copies of any free writing prospectus and it retains the ability to halt the use of any prospectus. Rule 433 requires that the free writing prospectus include a legend indicating where a prospectus is available and recommending that it be read. Other legends and disclaimers are prohibited. An immaterial or unintentional failure to include the legend can be cured, if a good faith effort was made to comply with the legend requirement, the legend is included as soon as practicable and it is retransmitted to the recipients of the free writing prospectus that omitted the legend.

When is the free writing prospectus filed?

The free writing prospectus generally must be filed on or before the day of first use. Issuers and other offering participants have separate obligations to file. Several exceptions apply, such as where there is no substantive change from a previously filed form of free writing prospectus, or the information is contained in the statutory prospectus, or the information is only the preliminary terms of the offered securities. Special two-day filing rules apply to free writing prospectuses that contain the final terms of the securities or the offering. Issuers may cure any immaterial or unintentional failure to file a free writing prospectus, if a good faith effort was made to comply with the filing requirement and it is filed as soon as practicable.

How do the new rules treat road shows? How about electronic road shows?

The new rules create no difficulties for traditional road shows, which are considered oral offers and thus have no filing requirement. To qualify as an oral offer, a road show must be presented live, in real time, to a live audience, even if all or part of it is transmitted electronically. Road shows that are not live, in real-time to a live audience are considered written communications, so they would be treated as free writing prospectuses. Graphics that are transmitted as part of a road show are treated the same way as the road show is treated—so graphics (such as slides) that only accompany a live road show are not written communications and need not be filed. Electronic road shows that would be free writing prospectuses are generally not required to be filed. The exception occurs in the case of an IPO, where the SEC seeks to encourage more visibility for road show presentations. An electronic road show in connection with an IPO must be filed unless the issuer company makes a version of it available electronically without restriction. The available electronic road show must be a bona fide version but need not be identical to other versions, and need not provide an opportunity for questions to be answered.

How are materials on a company website treated under the new rules?

If a company utilizes its website as part of the securities offering, the material utilized will have to be filed like other free writing prospectuses. Website information that is not part of the offering is not required to be filed. Historical information on the website will not be considered an offer, and so will not be a free writing prospectus, if it is identified and segregated in an archive section of the website and is not incorporated into the offering prospectus or otherwise referred to or used in the offering.

How do the new rules affect communications with the media?

In the past, communications with the media risked creating written material that could be deemed an illegal offer (i.e., a non-compliant prospectus) that violated the gun-jumping rules. Under the new rules, the SEC recognizes the important role of the financial media in communicating information to the marketplace, but seeks to prevent issuers from avoiding responsibility for their offerings by conducting an offer through the media. This balance is achieved by treating as a free writing prospectus of the issuer any media publication

that constitutes an "offer" and that arises out of information about the issuer or offerings provided by the company.

Filing, legend, record retention and prospectus availability requirements may apply under different circumstances.

Notably, if a chief executive officer gives an interview to an unaffiliated financial reporter after the filing of a regulation statement, the company is only required to file the resulting article as a free writing prospectus. No prospectus delivery requirement would apply.

Even where the company prepares or pays for media publications, the publication would simply be treated as a free writing prospectus. For seasoned issuers that are not well-known seasoned issuers, a statutory prospectus (which could be a base prospectus for a shelf offering) would have to be on file with the SEC at the time the paid media communication was published. Filing as a free writing prospectus under these circumstances would be required on or before the day of first use. Because any free writing prospectus of an unseasoned and non-reporting issuer must be accompanied or preceded by a copy of the statutory prospectus, these issuers will not be able to pay for or prepare media publications in connection with their securities offerings (except in compliance with Rule 134).

What liabilities are associated with a free writing prospectus?

Free writing prospectuses create potential liability just as statutory prospectuses do. A free writing prospectus, which represents information that is part of the offer but not part of a registration statement, will be subject to Section 12(a)(2) and Section 17(a)(2) liability, but not to Section 11 liability, for misstatements and omissions. The same is true for oral statements made as part of road show presentations.

The fact that information appears in a free writing prospectus and not in a statutory prospectus does not by itself mean there is a deficiency in the statutory prospectus or registration statement.

All free writing prospectuses that are used but not filed must be retained for three years by the issuer or other offering participant that used them.

How are the communications rules for the post-effective period different?

There is no change in the rules regarding communications made after the registration statement for an offering is declared effective. Free writings continue to be permitted. However, new developments in the offering process, including a new "access equals delivery" rule for final prospectuses, are likely to change the way many issuers and other offering participants communicate with investors.

Do these liberalized communications rules apply in the context of mergers and other business combination transactions?

No. Rules governing communications related to business combination transactions were modernized in connection with Regulation M-A in 1999. These rules were not revised in the recent securities reforms. However, companies that raise capital in a registered public offering in order to finance a business combination can rely on the securities offering rules and the Regulation M-A rules in tandem. If a communication relates to both a capital formation and a business combination transaction, it may be subject to both sets of rules.

Do the new rules modify Regulation FD?

Yes. Regulation FD formerly did not apply to communications in connection with most registered public offerings. Now it has been amended to specify the particular communications associated with public offerings to which it does not apply. Regulation FD does not apply to filed registration statements and the prospectuses they contain, post-filing free writing prospectuses, Rule 135 notices and Rule 134 communications, and post-filing oral communications. Other communications, such as regularly released factual business information or regularly released forward-looking information, remain subject to Regulation FD.

How are research reports by stock analysts affected by these rules?

Securities Act Rules 137, 138 and 139 contain safe harbor provisions permitting brokers and dealers to publish

securities research around the time of a registered public offering without violating Section 5 of the Securities Act. The rules include a definition of the term "research report" and a general loosening of the requirements for these safe harbors. These safe harbors are available for broker-dealers, not for issuers, so companies should be careful not to hyperlink to research reports around the time of a registered offering. Otherwise, the company would be deemed to have adopted the report, and it would become a free writing prospectus with associated liabilities for the company.

REGISTRATION PROCEDURES

What new shelf registration procedures apply to issuers generally?

Formerly, eligible issuers could register an amount of securities reasonably expected to be offered and sold within two years. Now, a shelf registration statement can be used for three years (with a limited extension), and shelf registrations are not limited in the amount to be registered. A new filing is required every three years, and unsold securities and fees can be rolled forward. Companies other than well-known seasoned issuers are still required to wait for the SEC staff to declare the registration statement effective.

Some procedural impediments that have disrupted offerings from time to time in the past have been eliminated. For instance, immediate take-downs off the shelf are permitted, and limitations on primary "at-the-market" offerings by eligible issuers have been eliminated. Selling security holders may now be identified and added using a prospectus supplement, not only by means of a post-effective amendment.

How do the new rules govern what offering information is included in a base prospectus or elsewhere?

New Rule 430B provides that the base prospectus in a shelf registration statement may omit information that is unknown or not reasonably available to the company. If selling security holders are participating in a registered offering along with the company, the identities of the selling securityholders may also be omitted if certain conditions are met.

To meet the requirements of a final prospectus, the company must make sure that information omitted from the base prospectus is included in a prospectus supplement, a post-effective amendment to the registration statement, or an Exchange Act report that is incorporated by reference into the registration statement (and specifically identified in a prospectus supplement). Form S-3 will permit seasoned issuers to incorporate by reference all information about the company and its securities (thus avoiding the need for a post-effective amendment to the registration statement). Information so omitted from the prospectus at the time it is declared effective that is subsequently contained in a prospectus filed with the SEC will be deemed part of the registration statement as of the day of first use or, if earlier, the time of first contract of sale.

What is the new automatic shelf registration process that is available for well-known seasoned issuers?

Under the new rules, well-known seasoned issuers are afforded the greatest latitude in registering and marketing securities, including the ability to register unspecified amounts of securities on immediately effective shelf registration statements. For a well-known seasoned issuer, the base prospectus may omit information that is unknown or not reasonably available. It may also omit information as to whether it is for a primary or secondary offering, the plan of distribution, and a description of the securities. The description of securities to be offered off the shelf may be as general as "common stock," "preferred stock" and "debt." Additional classes of securities can be added freely, and the registration statement can be used for both primary and secondary offerings. Filing fees will be on a "pay-as-you-go" basis at the time of each shelf takedown. Virtually all information about the company and any offering may be omitted from the base prospectus, to be added later by post-effective amendment, prospectus supplement or Exchange Act filing. The supplements and incorporated reports will be deemed to be part of the registration statement. Automatic shelf registration is not available for business combination transactions or exchange offers.

Are there any other changes to registration statement requirements?

Yes. Form S-1 now permits historical use of incorporation by reference to Exchange Act filings (but not forward

incorporation, which Form S-3 permits). Form S-1 incorporation by reference is available for all issuers (other than ineligible issuers) that have filed an annual report on Form 10-K and are current (not necessarily timely) on their reporting obligations, and that make their Exchange Act reports accessible on their websites.

Form S-2 has been eliminated.

How has prospectus delivery been modernized?

The Securities Act requires delivery of a final prospectus to each investor in a registered offering. Historically, after effectiveness of the registration statement, written confirmations of sale have been provided, but they must be accompanied or preceded by the final prospectus. Investment decisions are typically made before delivery of any final prospectus, and purchasers in the aftermarket do not receive final prospectuses (except in the case of dealer delivery requirements for 25 days after an IPO).

Under the new rules, sales may be confirmed without concurrent or prior delivery of a full prospectus—timely access is deemed equivalent to delivery of the final prospectus, or "access equals delivery." Filing the final prospectus with the SEC and complying with other conditions will satisfy the final prospectus delivery requirements. Purchasers may still request physical delivery of a final prospectus. As discussed below, potential liability is determined in light of the information conveyed to the investor at the time of the investment decision, so the final prospectus is not relevant to that determination.

EXCHANGE ACT REPORTING

Have Form 10-K disclosure requirements changed?

Yes. In recent years, many companies have disclosed risk factors in their periodic reports as a matter of good practice, often as part of management's discussion and analysis or the business discussion. Now the SEC has amended Form 10-K to require such disclosure. New Form 10-K Item 1A requires disclosure responsive to Regulation S-K Item 503, namely a "discussion of the most significant factors that make the offering speculative or risky." The Form 10-K risk factors would be similar to what is found in the prospectus for a public offering, without the specific offering-related risks. The risk factors must be written in the "plain English" style.

Quarterly reports on Form 10-Q would reflect only material changes to this disclosure. The SEC discourages unnecessary restatement or repetition of risk factors in quarterly reports. The adopting release notes that each reporting company is already required to undertake a quarterly review of its operations, financial results and other circumstances, and that the company's disclosure controls and procedures and internal control over financial reporting should be capable of alerting it to changing material risks.

Are we required to disclose unresolved SEC staff comments?

Yes. Form 10-K Item 1B requires accelerated filers and well-known seasoned issuers to report material written comments made in connection with an Exchange Act review that SEC staff issued more than 180 days before the end of the fiscal year but that remain unresolved as of the date of filing of the Form 10-K.

LIABILITY ISSUES

How do the new rules affect Section 11 liability?

Under Section 11 of the Securities Act, the issuer company and its directors, officers signing the registration statement, auditors and other experts, and the underwriters in the offering, have liability for untrue statements of material facts or omissions of material facts required to be included in a registration statement or necessary to make the statements in the registration statement not misleading at the time the registration statement becomes effective.

Prior to the new rules, determining the timing of liability under Section 11 could sometimes be an issue. For example, a prospectus supplement used after a shelf registration statement was declared effective was not obviously subject to Section 11 liability. The new rules deem prospectus supplements to be part of the registration statement to which they pertain, and therefore subject to Section 11 liability (in addition to Section 12(a)(2) liability discussed below). In shelf offerings, a prospectus supplement will be retroactively deemed part of the registration statement as of the earlier of the date of first use or the date and time of the first contract

for sale. Date of first use is the date when the prospectus is first available to a managing underwriter, syndicate member or prospective purchaser in the offering.

The new rules also change the date when Section 11 liability is determined. Previously, the liability of different participants in a shelf offering was assessed at different points in time. Liability of the issuer, signing officers, directors and experts was assessed at the later of the effective date of the registration statement or the date of the most recent annual report on Form 10-K. For underwriters, liability was assessed at the time they become underwriters for the offering, which could be long after the effective date of a shelf registration statement. Under the new rules, liability for both the issuer and the underwriters of an offering is determined as of the date of the shelf takedown. Liability for other participants (signing officers, directors and experts) is still determined as of the effective date of the registration statement, or if later, the date of the most recent annual report on Form 10-K. Among other things, this should mean that new auditor consents are not needed for the shelf takedown, and that directors will not be liable for the contents of a prospectus supplement on an overnight financing that they may not have had an opportunity to review.

How do the new rules affect Section 12(a)(2) liability? Section 17(a)(2) liability ?

Under Section 12(a)(2) of the Securities Act, a person who offers or sells securities may have liability to the purchaser for offers and sales by means of a prospectus or oral communication that includes an untrue statement of material fact or omits to state a material fact necessary to make the statements, in light of the circumstances under which they were made, not misleading. Section 17(a) is a general anti-fraud provision which provides, among other things, that it is unlawful for any person in the offer and sale of a security to obtain money or property by means of any untrue statement of a material fact or any omission 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.

A new interpretive rule adopted as part of the securities offering reforms clarifies that the issuer in a primary offering will always be considered a "seller" under Section 12(a)(2) with respect to registration statements, prospectuses, free writing prospectuses prepared on its behalf, and material information about the company or its securities that is provided by the company and contained in another person's free writing prospectus.

Free writing prospectuses are subject to Section 12(a)(2) liability, but not Section 11 liability (unless actually included in a registration statement or in an Exchange Act report that is incorporated by reference into a registration statement).

New Rule 159 codifies the SEC's position that liability is determined at the time of sale, based on information that is "conveyed" to the investor at the time of sale. In determining Section 12(a)(2) and Section 17(a)(2) liability with respect to the contents of a prospectus or oral communication, information conveyed to the investor only after the time of sale should not be considered. Information conveyed only in a final prospectus, prospectus supplement or Exchange Act filing that is filed or delivered after the contract for sale would not be considered in determining whether there was an untrue statement of a material fact or omission of a material fact in the information upon which the investor based a decision to purchase the securities. The term "conveyed" is not defined, and will be determined based on facts and circumstances, but it seems clear that investor access to the information alone will not always suffice.

If material information develops after the investment decision is made, seller and buyer may rescind the contract for sale and, following disclosure, enter into a new contract of sale. As a result, before pricing a transaction, underwriters and companies will want to complete due diligence and consider whether any "Recent Developments" disclosure is required to be conveyed to investors prior to sale. Final terms of the securities must be disclosed to investors prior to sale.

How might these changes affect issuer and underwriter offering practices?

We expect that securities offering practices are likely to evolve after a period of experimentation.

To begin with, it is advisable for issuers and underwriters, who share an interest in managing the disclosures made in connection with an offering, to agree on the plan for all communications to be used in connection with the offering.

Since liability determinations will be based on information conveyed as of the time of sale, and not any updated

information that may appear in a final prospectus delivered to investors or in Exchange Act reports filed after the time of sale, there should be a greater focus in any offering on ensuring that the preliminary prospectus and any free writing prospectus contains all information necessary for an investor to make an informed investment decision.

Issuers and underwriters in public offerings should consider making a record of the information conveyed to each investor, and at what time. In addition to the statutory prospectus, information could be provided orally in an amended preliminary prospectus, or in emails or other written communications (which are likely to be free writing prospectuses). Care should be taken to convey information in time for the investor to consider the new information before committing to purchase the securities.

Companies should also be mindful of Rules 408 and 12b-20, which mandate the inclusion of any material information that may be necessary to make the required statements, in light of the circumstances under which they are made, not misleading.

To discuss how these rules apply to your company, please contact any member of your Fenwick & West team. You may also contact Horace Nash (hnash@fenwick.com), Dan Winnike (dwinnike@fenwick.com) or Laird Simons (lsimons@fenwick.com), each of whom contributed to the preparation of this update, or send an inquiry to: fwcsu@fenwick.com.

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GLOSSARY

Free Writing Prospectus: Any "written communication" (see definition below), constituting an offer to sell or a solicitation of an offer to buy the securities in a registered offering, that is used after the registration statement for that offering is filed (or, for a well-known seasoned issuer, even before filing) and that is not a communication made through a final prospectus or one of several permitted forms of preliminary prospectus. Communications that an issuer provides under current safe harbors, such as Rules 134 and 135, and safe harbors under new Rules 168 and 169 for factual business information and forward-looking information, are excluded from the definition of free writing prospectus because those safe harbors define the covered communications not to be prospectuses or offers.

Graphic communication: Includes all forms of electronic media, including audiotapes, videotapes, facsimiles, CD-ROM, electronic mail, Internet websites, and substantially similar messages widely (not individually) distributed on voice mail systems or computers. Excluded from the definition of graphic communication, and thereby excluded from the definition of written communication, is any communication that "at the time of the communication, originates live, in real-time to a live audience and does not originate in recorded form or otherwise as a graphic communication, although it is transmitted through graphic means."

Ineligible Issuer: An issuer that is:

- a reporting company that has not made all required SEC filings during the prior year, other than some excludable Form 8-K filings; or
- an issuer that is (or, including predecessors, in the past three years was):
  - » a blank check company;
  - » a shell company; or
  - » an issuer of penny stock; or
- an issuer with respect to which a petition under the federal bankruptcy laws was filed within the past three years; or
- an issuer that is otherwise excluded by the definition in Rule 405 under the Securities Act.

Non-Reporting Company: A company that is not required to file Exchange Act reports (commonly, a company that is conducting its initial public offering).

Reporting Company: A company that is required to file Exchange Act reports. A reporting company may be an unseasoned issuer, a seasoned issuer, or a well-known seasoned issuer.

Seasoned Issuer: A company that is required to file Exchange Act reports and is eligible to use Form S-3 to conduct primary offerings of securities.

Unseasoned Issuer: A company that is required to file Exchange Act reports but is not eligible to conduct a primary offering on Form S-3 (for example, a company that has been required to file Exchange Act reports for less than a year).

Voluntary Filer: A company that is not required to file Exchange Act reports but does so voluntarily.

Well-Known Seasoned Issuer: An issuer that:

- meets the registrant requirements of Form S-3, General Instruction 1.A (generally, having been a reporting company for at least a year and having made all required SEC filings in a timely manner during the prior year, other than some excludable Form 8-K events); and
- has either
  - » a market value of its common equity held by nonaffiliates of at least $700 million, or
  - » in the last three years has issued at least $1 billion principal amount of nonconvertible securities, other than common equity, in primary offerings for cash, not exchange, in registered offerings under the Securities Act; and
- is not an ineligible issuer (see definition above).

An issuer's status as a well-known seasoned issuer is determined as of the latest of:

- the date of filing of the issuer's most recent shelf registration statement;
- the date of the issuer's most recent amendment (by post-effective amendment, incorporated Exchange Act report or form of prospectus) to a shelf registration statement; or
- the date of filing of the issuer's most recent annual report on Form 10-K (for issuers that have not filed a shelf registration statement or amendment for 16 months).

Written Communication: Any communication that is written, printed, a radio or television broadcast, or a graphic communication.

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