

**SEC Adopts New Rules to Facilitate Changing Between Public and Private Offerings**

March 7, 2001

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On January 26, 2001, the Securities and Exchange Commission adopted a new rule governing the integration of abandoned offerings. New Rule 155 is intended to facilitate changing an offering from a private offering to a registered public offering, and *vice versa*, to accommodate the rapidly changing dynamics of the capital markets. New Rule 155 became effective on March 7, 2001.

Set forth below is a brief summary of the SEC's integration doctrine and the key provisions of new Rule 155.

**SEC's Integration Doctrine**

The SEC's integration doctrine furnishes a framework for determining whether multiple securities transactions should be *integrated* and considered as part of the same offering.<sup>1</sup>

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<sup>1</sup> Integration of Abandoned Offerings, SEC Release No. 33-7943 (January 26, 2001).

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The SEC has traditionally applied a five-factor test in evaluating whether such transactions should be integrated.<sup>2</sup> Although the SEC has created some safe harbors from integration,<sup>3</sup> and has provided no-action relief from integration in limited circumstances,<sup>4</sup> none of the SEC's prior rules, safe harbors or staff interpretations addressed the situation where an issuer either:

- commences a private offering, abandons it before any securities are sold, and then files a registration statement to commence a public offering;<sup>5</sup> or
- files a registration statement, withdraws the statement before any securities are sold, and then commences a private offering to raise capital.

Arguably, either one of these scenarios raises integration concerns under the SEC's five-factor test.

### **Abandoned Registered Offering Followed by a Private Offering**

Under the SEC's prior rules, an issuer who withdraws an effective registration statement must wait six months before initiating a private offering.<sup>6</sup> Recognizing that an issuer may

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<sup>2</sup> *Id.* The five factors relevant to the question of integration are as follows:

1. Are the offerings part of a single plan of financing?
2. Do the offerings have the same general purpose?
3. Are the offerings of a same class of securities?
4. Are the offerings made at or about the same time?
5. Are the securities sold for the same type of consideration?

For the SEC's interpretive releases identifying these five factors, see SEC Release No. 33-4434, 26 FR 11896 (Dec. 6, 1961) and SEC Release No. 33-4552, 27 FR 11316 (Nov. 6, 1962).

<sup>3</sup> Other integration safe harbors include: Rule 502(a), 17 C.F.R. 230.502(a)(Regulation D offerings); Rule 147(b)(2), 17 C.F.R. 230.147(b)(2)(for exempt state offerings); Rule 251(c), 17 C.F.R. 230.251(c)(for small offerings by non-reporting issuers under Regulation A); and Rule 701(f), 17 C.F.R. 230.701(f)(for non-reporting issuers' exempt offerings to employees and consultants under written compensatory benefits. Integration of Abandoned Offerings, SEC Release No. 33-7943 (January 26, 2001).

<sup>4</sup> In two separate SEC no-action letters, the SEC permitted the use of concurrent public and private offerings in very limited circumstances. The SEC emphasized, however, that such relief was available as long as the private offering was limited to "qualified institutional buyers" as defined under Rule 144A of the Securities Act and a small number of large institutional accredited investors. See e.g., Black Box Incorporated, SEC No-Action Letter (June 26, 1990)("Black Box"); and MB Holdings Inc., SEC No-Action Letter (Feb. 28, 1992)(**Squadron Ellenoff**).

<sup>5</sup> If an issuer has already completed a private offering, the issuer cannot rely on the Rule 155 safe harbor. According to the SEC, however, Rule 152 of the Securities Act (and the SEC's related interpretations), which generally allows an issuer to initiate a registered public offering after the issuer has completed a private offering, is unaffected by the Rule 155 safe harbor.

<sup>6</sup> The SEC staff has traditionally viewed the filing of a registration statement as a general solicitation. If a subsequent private offering was considered to be integrated with a withdrawn public offering, the general solicitation would most likely defeat an issuer's claim to any private offering exemption, thus forcing the issuer to wait six months in order to avoid any integration concerns. Integration of Abandoned Offerings, SEC Release No. 33-7943 (Jan. 26, 2001).

discover insufficient investor interest to proceed with the registered public offering but may still need to raise capital rather quickly, the SEC adopted Rule 155(c) under the Securities Act to provide issuers with a safe harbor from integration. Under Rule 155(c), an offering for which an issuer has filed a registration statement will not be integrated with a later commenced private offering if:

- No securities were sold in the registered offering;
- The issuer withdraws the registration statement under Rule 477 of Regulation C;<sup>7</sup>
- Neither the issuer or any person acting on the issuer's behalf commences the private offering earlier than 30 calendar days after the effective date of withdrawal of the registration statement under Rule 477 of Regulation C;<sup>8</sup>
- The issuer notifies each offeree in the private offering that:
  - The offering is not registered under the Securities Act;
  - The securities will be *restricted securities* (as defined in Rule 144(a)(3) under the Securities Act) and may not be resold unless they are registered under the Securities Act or an exemption from registration is available;
  - Purchasers in the private offering do not have the protection of Section 11 of the Securities Act; and
  - A registration statement for the abandoned offering was filed and withdrawn, specifying the effective date of the withdrawal; and
- Any disclosure document used in the private offering discloses any changes in the issuer's business or financial condition that occurred after the issuer filed the registration statement that are material to the investment decision in the private offering.

According to the SEC, Rule 155(c) should provide legal certainty for issuers who are hesitant to raise capital through private offerings after they have withdrawn a registration statement by eliminating any integration concerns. The new safe harbor, together with the amendments to Rule 457 discussed below, should also assist issuers by reducing some of the costs associated with the abandoned registered offering process, as previously described above.

### **Abandoned Private Offering Followed by a Registered Public Offering**

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<sup>7</sup> The SEC has also amended Rule 477 to facilitate the process of withdrawing a registration statement. Under the amended rule, an application for the withdrawal of an entire registration statement made before the registration becomes effective will be deemed granted upon filing unless, within 15 calendar days after the issuer files the application, the SEC notifies the issuer that the application will not be granted. 17 C.F.R. 230.477(b).

<sup>8</sup> An issuer may not use the Rule 155(c) safe harbor unless the subsequent private offering is made pursuant to an exemption under Section 4(2), Section 4(6) or Rule 506 under the Securities Act. Integration of Abandoned Offerings, SEC Release No. 33-7943 (Jan. 26, 2001).

If an abandoned private offering was followed by a registered public offering, the SEC or the courts could find the issuer in violation of Section 5(c) of the Securities Act as a result of the offers made prior to the filing of the issuer's registration statement. New Rule 155(b) under the Securities Act, however, provides a safe harbor from integration that allows an issuer to abandon the private offering and to initiate a registered public offering, without having to wait six months to file the registration statement.<sup>9</sup> The safe harbor may be particularly useful where an issuer has encountered a favorable response to a private offering from investors, and would like to switch to a registered offering. Rule 155(b) provides that a private offering of securities will not be integrated with an offering for which the issuer later files a registration statement if:

- No securities were sold in the private offering;<sup>10</sup>
- The issuer and any person(s) acting on its behalf terminate all offering activity in the private offering before the issuer files the registration statement;
- The preliminary and final prospectuses used in the registered offering disclose information about the abandoned private offering, including:
  - The size and nature of the private offering;
  - The date on which the issuer abandoned the private offering;
  - That any offers to buy or indications of interest given in the private offering were rejected or otherwise not accepted; and
  - That the prospectus delivered in the registered offering supercedes any offering materials used in the private offering; and
- The issuer does not file the registration statement until at least 30 calendar days after the termination of all offering activity in the private offering, unless the issuer and any person acting on its behalf offered securities in the private offering only to persons who were (or who the issuer reasonably believes were):
  - Accredited investors (as defined under Rule 501(a) of Regulation D);  
or
  - Persons who satisfy the knowledge and experience standard of Rule 506(b)(2)(ii) of Regulation D.

The SEC intends to monitor the use of Rule 155(b) carefully in order to prevent any misuse by issuers. According to the SEC, this monitoring may take the form of Staff requests for

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<sup>9</sup> The SEC staff has traditionally applied the six-month non-integration safe harbor of Regulation D even if the private offering does not rely on Regulation D for an exemption. Integration of Abandoned Offerings, SEC Release No. 33-7943 (January 26, 2001).

<sup>10</sup> In order for an issuer to rely on the Rule 155(b) safe harbor, the abandoned offering must have been made pursuant to an exemption from registration under Section 4(2), Section 4(6) or Rule 506 under the Securities Act. An issuer may not use Rule 155(b) if the issuer relied exclusively on the SEC's exemption provided by Rule 505 of the Securities Act. *Id.*

supplemental information regarding the termination of all offering activity in the private offering.<sup>11</sup>

### **Amendments to Rule 457**

In order to further reduce the costs associated with a withdrawn registration statement, the SEC has also amended Rule 457 (computation of fee) to permit filing fees to be offset from withdrawn registration statements. The amended rule provides that where all or a portion of the securities offered under a registration statement remain unsold after the withdrawal of a registration statement (or after the completion or termination of the registered offering), the aggregate total dollar amount of the filing fee associated with those unsold securities may be offset against the total filing fee due for a subsequent registration statement or statements.<sup>12</sup> Significantly, any filing fee offset must occur within five years of the initial filing date of the earlier registration statement and must be filed by the same registrant (including a successor as defined under Rule 405 of Regulation C), a majority-owned subsidiary of that registrant, or a parent that owns more than 50 percent of the registrant's outstanding voting securities.<sup>13</sup>

### **The Effect of Rule 155 on Existing Safe Harbors and the SEC's Integration Interpretations**

As stated earlier, Rule 155 is intended to provide an additional safe harbor to integration for the specific situations described above and thus does not affect, change or alter any of the existing safe harbors under Regulation D. Moreover, the SEC has emphasized that Rule 155 does not alter, restrict or limit the SEC's existing *Black Box* no-action letter interpretations,<sup>14</sup> nor does the rule affect the traditional five-factor analysis for integration.

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<sup>11</sup> Integration of Abandoned Offerings, SEC Release No. 33-7943 (Jan. 26, 2001).

<sup>12</sup> 17 C.F.R. 230.457(p).

<sup>13</sup> *Id.*

<sup>14</sup> In its adopting release for Rule 155, the SEC emphasized that Rule 155 does not affect the SEC's policy position with respect to concurrent private and registered offerings that was articulated in *Black Box* and *Squadron*. Integration of Abandoned Offerings, SEC Release No. 33-7943 (January 26, 2001).