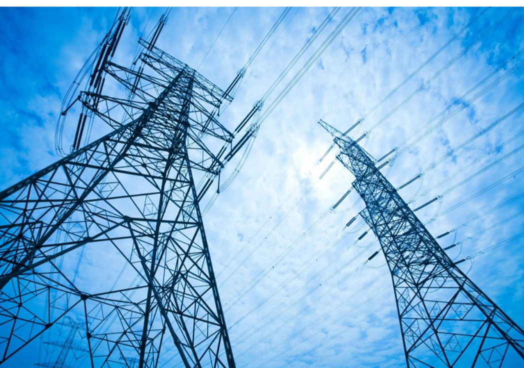
HUNTON
ANDREWS KURTH

BASELOAD

Current Topics in the Power and Utilities Capital Markets



October 2022

Contents

Weighing the Options: A Guide to Greenshoes **1**

Bloomberg Blasts: Practical and Legal Considerations for Registered Debt Deals......... **8**

Dark Company Debt: 15c2-11 Changes May Soon Be Coming......................... **12**

Weighing the Options: A Guide to Greenshoes

Introduction

In certain equity and equity-linked offerings, the underwriters often negotiate for a provision in the underwriting agreement whereby the issuer grants to the underwriters an option to purchase additional securities (of the same type) from the issuer.[1] This option, historically known as a "greenshoe option", was named for The Green Shoe Manufacturing Company, which first used the option in connection with a 1963 secondary offering of common stock.[2]

Greenshoe options are utilized for various reasons. Sometimes greenshoe options are exercised to increase the aggregate amount of proceeds to the issuer from the offering. Other times, greenshoe options are utilized to stabilize the price of the security after pricing. Greenshoe options are sometimes exercised to satisfy demand from investors.

For purposes of this article, the term "greenshoe option" will be used to include both a traditional "overallotment" option and a "refreshable shoe" option. As this article will attempt to make clear, however, both options are executed differently, serve different purposes, can be treated differently for liability purposes and require specialized disclosure and contractual language.

1 Greenshoe options are also utilized in 144A/Reg S transactions. For simplicity's sake, this article will use general terms such as "underwriter", "prospectus supplement" and "underwriting agreement" without mentioning the corresponding term in 144A/Reg S transactions. Certain securities laws ramifications of exercising a greenshoe option, however, are not applicable to 144A/Reg. S transactions given the unregistered nature of such issuances.

2 Given the industry focus of Baseload, this article will only analyze greenshoe options in connection with offerings by listed issuers.

Traditional Overallotment Option

The traditional greenshoe overallotment option is granted to the underwriters and exercised by the underwriters ***solely to cover sales of overallotted securities made before "syndicate breaks"*** – i.e., the time when formal fixed price sales and secondary trading restrictions are lifted by the managing underwriter. We refer to this as the "traditional overallotment" option.

Post-pricing stabilization (short-covering) by an underwriter generally occurs as follows:

- The underwriter (which is also acting as stabilization agent) prices the deal and establishes a syndicate short position on the pricing date by overalloting the securities;
- The underwriter breaks syndicate and sends the termination wire to the underwriting syndicate;
- The securities trade below the offering price in the after-market; and
- The underwriter, on behalf of the underwriting syndicate, buys in the open market an amount of the offered securities that is less than or equal to the syndicate short position at prices below the offering price and, in so doing, reduces the size of the syndicate short position (or eliminates the syndicate short position altogether).

However, if the underwriter is unable to cover the syndicate short position in the open market (including if the securities trade above the offering price) the underwriter will exercise the traditional overallotment option.

Refreshable Shoe Option

As equity capital markets have become more sophisticated since the 1963 Green Shoe Manufacturing issuance, various other greenshoe options have developed. A popular greenshoe option in today's equity capital markets is known as a "refreshable shoe." Similar to a traditional overallotment option, underwriters will negotiate for this option in the underwriting agreement to be able, at their option, to purchase additional securities from the issuer. Unlike the traditional overallotment option, however, the "refreshable shoe" option allows the underwriter (which is also acting as stabilization agent) to use greenshoe option securities ***to cover the syndicate short position entered into after syndicate breaks***.

The exercise of a "refreshable shoe" option typically involves the following series of events:

- The underwriter prices the deal and establishes a syndicate short position on the pricing date by overalloting the securities (and the syndicate is terminated);
- The securities trade below the offering price in the after-market;
- The underwriter makes purchases, on behalf of the underwriting syndicate, of the securities in an amount less than (or equal to) the syndicate overallotment short position in the open market and holds those securities for the syndicate (i.e., the securities are not used to close out the syndicate short position);
- The price of the securities subsequently rises and the underwriter sells the securities previously purchased in the open market on behalf of the underwriting syndicate, thus "refreshing" the size of the syndicate overallotment short position;
- The underwriter exercises the greenshoe option at or after the time of such refreshing sales to cover the syndicate short position re-established by such refreshing sales.

Note that the refreshable shoe is almost never exercised in an amount that exceeds the syndicate short position. See "Legal Considerations and Reg. M" below.

Size

The size of the greenshoe option (whether a traditional overallotment option or a refreshable shoe) is generally set at 15% of the securities to be offered. There is a corresponding size limit set forth in FINRA Rule 5110(g)(9), among a list of deal terms that FINRA deems to be "Unreasonable Terms and Arrangements".

When sizing the deal, issuers ought to keep in mind the potential for a 15% upsize pursuant to the greenshoe option. Such upsize, however, cannot be guaranteed by the underwriters. To avoid uncertainty, issuers and underwriters are advised to discuss the greenshoe option in terms of overall deal sizing early in the deal process.

Duration

The typical greenshoe option has a duration of 30 days from the date of the underwriting agreement. The Division of Corporation Finance takes the position that overallotment options with terms of more than 45 days will trigger the shelf registration provisions of Rule 415: [3]

> **Question**
>
> In what circumstances does an over-allotment offering constitute a delayed offering such that compliance with Rule 415 is necessary?
>
> **Answer:**
>
> As a matter of administrative practice, over-allotment options with terms of up to 45 days may be made without triggering compliance with Rule 415.

Rule 15c3-3(d)(4) under the 1934 Act also requires certain short positions to be closed out within 30 days; provided, however, that per such rule, the 30-day period does not start to run until the completion of an underwriter's participation in the distribution.

In our experience, the duration of the greenshoe option may be negotiated. For example, in some common stock follow-on offerings, issuers have negotiated a greenshoe option pursuant to which any exercise by the underwriters is required to close concurrently with the initial offering. Such a "close everything at once" scenario can provide administrative and procedural ease given that a standalone greenshoe closing will require updated legal opinions (including 10b-5 negative assurance statements) and comfort letter.

Documentation

It is critical to document accurately the specific type of the greenshoe option that will be utilized in the offering:

- **Underwriting Agreement:** If utilizing the "refreshable shoe" option, the underwriting agreement cannot limit the greenshoe option to covering overallotments. Typical "refreshable shoe" language states: "The Corporation hereby grants to the underwriters the option to purchase from time to time all or any part of an additional XXX shares of common stock, subject to certain conditions set forth herein." "Traditional overallotment" language usually provides as follows: "The Corporation hereby grants to the underwriters the right to purchase at their election up to XXX option shares, solely to cover overallotments, at the purchase price set forth above."

  Additionally, the underwriting agreement should make clear (regardless of the type of greenshoe option) whether multiple exercises of the greenshoe option are permissible. See the "refreshable shoe" language in the paragraph immediately above which permits multiple exercises of the option.

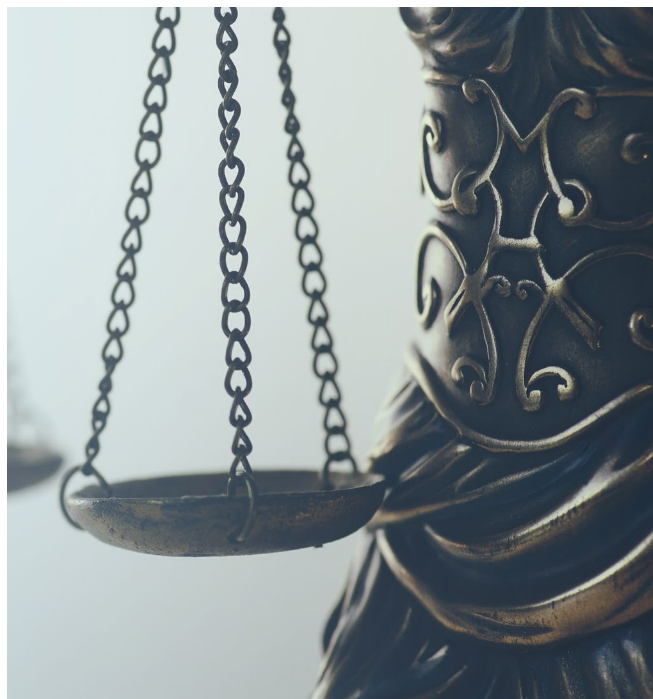
3 See Compliance and Disclosure Interpretations for the 1933 Act Rules, Question 212.01 *available at* https://www.sec.gov/corpfin/securities-act-rules.

- **Prospectus supplement:** Similar to the underwriting agreement, the prospectus supplement in a "refreshable shoe" transaction should not state that the greenshoe option is for covering overallotments. The typical disclosure for a traditional overallotment option or a "refreshable shoe" option should track the corresponding language in the underwriting agreement.

  Additionally, disclosure of the greenshoe option will appear on the cover of the prospectus supplement as well as in the "Underwriting" section. Moreover, Item 508(l) of Regulation S-K requires a description in the prospectus supplement of any transaction that an underwriter intends to conduct that stabilizes, maintains or otherwise affects the market price of the offering securities. Specifically, Item 508 requires information on stabilizing transactions, syndicate short covering transaction, penalty bids "or any other transaction that affects the offered security's price."

- **Opinions/Comfort Letter:** Legal opinions and comfort letters will be required to be delivered at the closing of the initial securities – and at any closing (or closings) of the applicable greenshoe option. But for the date of the delivery of the opinions and comfort letter, the subject matter of such legal and accounting letters should not differ from those delivered at the initial closing. Furthermore, the legal opinions and comfort letters do not distinguish between a traditional overallotment option or a "refreshable shoe" option. So, such documents can be relatively simple "bring-down" letters from those delivered at the initial closing.

  Deal participants, however, should be aware that if serial exercises of the greenshoe option are executed, there will be a "mini" closing with respect to each exercise and legal opinions (including 10b-5 negative assurance statements) and comfort letters will need to be delivered accordingly. To the extent that a greenshoe closing occurs during an issuer's "blackout" period, discussions on the timing of the delivery of the required documents (especially the comfort letter) prior to launching the initial issuance are highly recommended.



Diligence

As discussed above, legal opinions (including 10b-5 negative assurance statements) and comfort letters will be required at closing. Furthermore, as discussed later, for Regulation M purposes, the issuer may be deemed to be "in distribution" if making "refreshable shoe" sales. Accordingly, attorneys may need a bringdown diligence call (and underwriters may require such a call for their due diligence purposes) concurrently with a greenshoe exercise. Given that, in some cases, greenshoe options can be exercised up to 30 days after the initial closing, deal participants will need to remain vigilant with respect to material developments occurring within that 30 day timeframe.

Legal Considerations and Reg. M

Regulation M, which went into effect on March 4, 1997 (Reg. M) is intended to prevent manipulative practices by issuers and underwriters in securities offerings. Reg. M is a "prophylactic" rule, which means that it prohibits certain conduct whether or not that conduct actually violates the securities laws. The operative provisions of Reg. M generally prohibit underwriters (Rule 101 of Reg. M) and issuers (Rule 102 of Reg. M) from bidding for, purchasing or attempting to induce others to bid for or purchase securities during a restricted period while such securities are "in distribution" (i.e., while they are being offered). Once the distribution is terminated, these provisions of Reg. M no longer apply.[4]

4 For Reg. M purposes, the completion or participation in a distribution occurs when the securities subject to the distribution have been distributed and all stabilization arrangements and trading restrictions in connections with the distribution have been terminated.

Rules 101 and 102 contain a number of exceptions. Investment grade non-convertible debt and preferred stock are exempt. "Exempted securities" as defined in Section 3(a)(12) under the 1934 Act are exempt. Rule 144A/Reg S. transactions are exempt. Rule 101 (which applies to underwriters and similar distribution participants) provides an exemption (which is not present in Rule 102) for "actively-traded securities" (at least $150 million public float and $1 million average daily trading volume) as defined under Reg. M.

Despite its prophylactic nature, Reg. M does provide that bids and purchases will be permitted even while an overallotment option remains unexercised, provided that the option is not exercised "in an amount that exceeds the net syndicate short position at the time of such exercise". The SEC published the following Q&A: [5]

> **Question:**
>
> If the managing underwriter of a distribution intends to exercise an overallotment option granted in connection with the offering, when is the distribution considered completed?
>
> **Answer:**
>
> A syndicate member's participation in the distribution is completed when all of the securities have been distributed and after any stabilization arrangements and trading restrictions in connection with the distribution have been terminated. A later exercise of an overallotment option does not affect the "termination" of the distribution, unless it is exercised for an amount exceeding the syndicate short position at the time of exercise. In this case, the distribution would be deemed to continue until the time that all the excess shares were sold. If the syndicate agreement is terminated before all of the shares have been sold, a syndicate member's participation would be completed once its remaining shares are distributed and its financial interests in the offering are terminated.

5 Division of Trading and Markets: Staff Legal Bulletin No. 9 Frequently Asked Questions About Regulation M (November 22, 2019)

The SEC's Q&A above underscores the importance of the overallotment amount not exceeding the syndicate short position. If such amount did, in fact, exceed the syndicate short position, the "distribution" would not be terminated and, accordingly, the restricted period would still be in effect. Furthermore, while the securities are "in distribution", securities law liability will apply to the issuer and underwriters for "refreshable shoe" sales. Note also, for purposes of exercising a "refreshable shoe" option, the underwriters will require confirmation that an issuer's common stock qualifies under the "actively-traded securities" exemption under Reg. M.

Survey of Recent Utility Deals

Set forth below is a list of recent SEC-registered equity and equity linked deals in the utility industry, with corresponding data relating to each greenshoe option.

Common Stock (Follow-On)			
Company	**Closing Date**	**Greenshoe Option**	**Length**
Exelon Corp.	August 9, 2022	Refreshable Shoe	30 day
Allete, Inc.	April 5, 2022	Refreshable Shoe	30 day
Northwest Natural Holding Company	April 1, 2022	Refreshable Shoe	30 day
NorthWestern Corporation	November 19, 2021	Refreshable Shoe	30 day
Unitil Corporation	August 6, 2021	Refreshable Shoe	30 day
Consolidated Edison, Inc	June 18, 2021	No	n/a
South Jersey Industries, Inc.	March 22, 2021	Refreshable Shoe	30 day
SJW Group	March 11, 2021	Refreshable Shoe	30 day

Mandatory Convertible				
Company	**Closing Date**	**Greenshoe Option**	**Host**	**Length**
NextEra Energy, Inc.	September 14, 2022	No	Senior Notes	n/a
UGI Corporation	May 25, 2021	Traditional Overallotment	Convertible Preferred	30 day
NiSource Inc.	April 19, 2021	Traditional Overallotment	Convertible Preferred	13 day
South Jersey Industry, Inc.	March 22, 2021	Traditional Overallotment	Junior Subordinated Notes	13 day
Spire Inc.	February 16, 2021	Traditional Overallotment	Senior Notes	13 day

It should be noted that the "refreshable shoe" option is not available for registered (optional) convertible offerings or mandatory convertible offerings because the "actively-traded securities" exemption under Reg. M , which would apply to the common stock underlying such convertible security, will not provide an exemption for the particular convertible being offered. Accordingly, the Spire, South Jersey Industries, NiSource and UGI mandatory convertible offerings described in the table above provided for a traditional overallotment option.

Each of the Spire and South Jersey Industries mandatory convertible offerings provided for a 13-day greenshoe. We understand that one reason for the truncated greenshoe duration in the case of a mandatory convertible is tax-driven. Given that a mandatory convertible often contains a debt host, it's important that any subsequent sale of the debt component of the mandatory convertible (per the greenshoe option) be fungible with the debt that was part of the initial sale. By limiting the duration of the greenshoe as such, we understand that issuers can take advantage of a safe harbor for tax purposes (and ensure that the debt component of the unit sold in the greenshoe is fungible with the debt component of the unit sold in the initial sale.) See "Debt Reopeners: A Restated Utility Quick Reference" in the November 2021 Baseload. While the NiSource and UGI mandatories each included a convertible preferred host, they reached different conclusions about whether the 13-day greenshoe was preferable (with UGI permitting a 30-day option).

Finally, while greenshoe options are sometimes included in subordinated debt offerings, a recent review of subordinated debt offerings in the utility industry found that few issuers are including greenshoe options in such offerings. For a relatively recent example of a subordinated debt offering with a greenshoe option, see the retail "Series N" junior subordinated debentures of NextEra Capital Holdings, Inc. which closed on March 15, 2019.

Conclusion

The regulatory framework surrounding any greenshoe option is extensive. Considerations include, but are not limited to, Regulation M, FINRA rules, 1933 Act rules and 1934 Act rules, as well as the SEC's interpretations thereof. Putting the regulatory framework aside, the deal documents, including the underwriting agreement and offering document, will need to memorialize and disclose the exact scope of the option. And the participating underwriters will also likely have internal guidelines, both from their equity capital markets desk and legal departments, as to exactly what is required and/or expected.

What is not surprising is that greenshoe options often have different relevance and format in connection with the various securities most often issued by domestic utility systems. Whether it be follow-on equity offering, mandatory convertible, subordinated debt or otherwise, the associated concerns and market practice for a greenshoe option are often specific to each security.

Bloomberg Blasts: Practical and Legal Considerations for Registered Debt Deals

Prior to engaging in roadshow activities, bankers will typically send a notification to accounts regarding an issuer's upcoming marketing. These notifications are sent via Bloomberg and are referred to as "Bloomberg Blasts." Consisting of only a few paragraphs, Bloomberg Blasts typically contain the name and brief description of the issuer, the identities of the issuer's executives participating in the marketing sessions, securities laws legends and, where applicable, a very brief description of the securities to be offered. Bloomberg Blasts may be circulated at two different times—first, if applicable, to announce "non deal" marketing in the days before launching a deal and second, to announce the launch of the deal.

This article will consider the legal and practical considerations with respect to Bloomberg announcements in the context of an SEC-registered deal. In SEC-registered issuances, deal participants need to ensure Bloomberg Blasts do not trigger unintended liabilities or filing requirements.

Non-deal Bloomberg Blast

"Non deal" marketing is used in a number of circumstances, including:

- for infrequent issuers in the capital markets;
- for ESG-focused initiatives;
- for new corporate structures resulting from strategic transactions; or
- for new investor audiences.

We refer to the Bloomberg Blast announcing these "non deal" marketing efforts as the "Non-deal Bloomberg". Oftentimes, if market conditions are receptive and non-deal marketing efforts have been encouraging, issuers will consider accessing the capital markets soon after the completion of non-deal marketing. Given this possibility, deals participants must analyze a Non-deal Bloomberg under multiple constructs.

Is a non-deal Bloomberg an offer?

Section 2 of the Securities Act of 1933, as amended (1933 Act), defines offer as including:

> *every attempt or offer to dispose of, or solicitation of an offer to buy, a security*

The term "offer" has historically been interpreted very broadly. That said, if an issuer engages in non-deal marketing efforts with no imminent expectation of accessing the capital markets, a Non-deal Bloomberg, under the appropriate facts and circumstances, may not be deemed an "offer".

Does the Non-deal Bloomberg need to comply with Rule 134?

If there is a possibility that a deal may follow non-deal marketing activities, the securities law analysis of a Non-deal Bloomberg must contemplate such a possibility.

Rule 134 (which is entitled "Communications Not Deemed a Prospectus") under the 1933 Act provides that certain limited written communications related to an offering as to which a registration statement has already been filed will not be considered a prospectus (i.e., the communication will be exempt from SEC restrictions applicable to written offers). But Rule 134 is only available after a preliminary prospectus that meets the requirements of Section 10 of the 1933 Act has been filed (which includes a base prospectus in a shelf registration statement that covered the securities to be offered).

One important aspect of Rule 134 is that the Rule 134 safe harbor is limited to a delineated list of information, including (1) factual information about the legal identity and location of the issuer, (2) the title and amount of securities being offered, (3) a brief description of the business of the issuer, (4) the price of the security or the method for determining price, (5) for debt, the final maturity, interest rate or yield,

(6) the anticipated use of proceeds (if already disclosed in the prospectus on file with the SEC), (7) the names of the underwriters, (8) the schedule for the offering and a description of marketing events and (9) a required legend.

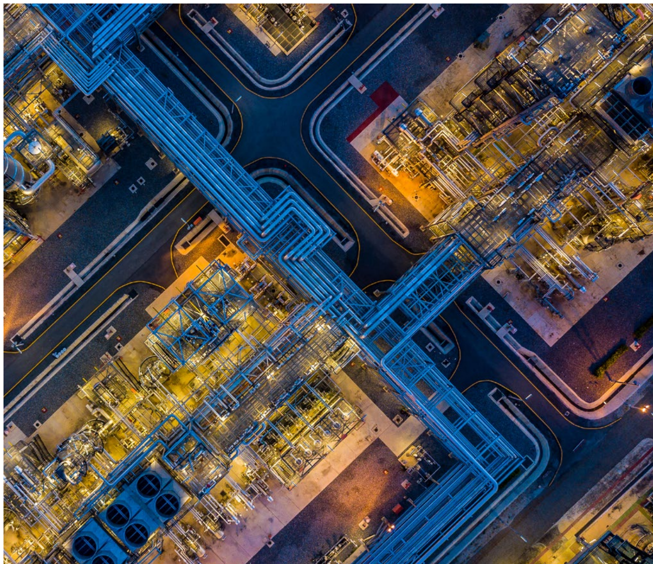
Note that one item that is not included in the above list is credit ratings. If the Bloomberg Blast contains credit ratings, the communication will fall out of the confines of Rule 134.

Historically, many deal participants attempted to restrict Bloomberg Blasts to the confines of Rule 134 in order to avail themselves of its safe harbor. Much like the analysis of electronic roadshows (see "Electronic Road Shows—What To Leave In, What To Leave Out" January 2014 edition of Baseload), however, the securities law analysis of Bloomberg Blasts has become more nuanced and many practitioners now believe that strict adherence to Rule 134 is no longer required.

Does Rule 433 apply to the Non-deal Bloomberg and, if so, is the Non-deal Bloomberg compliant?

A free writing prospectus (per Rule 405 under the 1933 Act) is any written communication that constitutes an offer to sell or a solicitation of an offer to buy the securities that are the subject of a registered offering and is used after a registration statement has been filed. The use of a free writing prospectus is governed by Rule 433 under the 1933 Act (as well as by Rule 164 under the 1933 Act).

Is the Non-deal Bloomberg a free writing prospectus subject to the requirements of Rule 433? If a deal does not ultimately follow non-deal marketing efforts, there is certainly a compelling argument that the announcement of non-deal marketing does ***not*** constitute an offer to sell securities.



Given the inherent uncertainty as to whether a deal will follow, however, most practitioners prefer to include some style of a Rule 433 legend as part of the Non-deal Bloomberg as a prophylactic measure.

Further, there is some difference in opinion among practitioners as to whether any 433-style legend included in the Non-deal Bloomberg should track the form of legend provided in Rule 433.[1] Specifically, as noted below, some practitioners prefer to include a legend referencing the possibility of an upcoming offering.

Related to this same point, some practitioners have focused on the presence, or absence, of language in the body of the Non-deal Bloomberg that a "deal may follow". Market practice has evolved over the years such that some Non-deal Bloombergs will include the phrase "A potential SEC-registered debt offering may follow, subject to market conditions." If the Non-deal Bloomberg discusses the possibility of a forthcoming deal, there is certainly a greater argument that the Non-deal Bloomberg may constitute an offer of securities and should contain a fulsome Rule 433 legend.

The question then becomes, if the Non-deal Bloomberg is an offer of securities (because of "deal may follow" language or otherwise) and is not limited in scope so as to take advantage of Rule 134, will the Non-deal Bloomberg constitute a ***compliant*** free writing prospectus under Rule 433?

There is an exception in Rule 433(d) as follows:

> (5) Notwithstanding the provisions of paragraph (d)(1) of this section:
>
> (i) To the extent a free writing prospectus or portion thereof otherwise required to be filed ***contains a description of terms of the issuer's securities in the offering or of the offering that does not reflect the final terms,*** [emphasis added] such free writing prospectus or portion thereof is not required to be filed;

So while the Non-deal Bloomberg may constitute a free writing prospectus, given the preliminary nature of any information relating to the deal contained therein, the free writing prospectus should, under most circumstances, not need to be filed.

Finally, one final practice point is to make sure the legending on any non-deal marketing slide deck generally lines up with the legend provided in the Non-deal Bloomberg.

1 See Rule 433(c)(2).

Deal Bloomberg

As with the Non-deal Bloomberg, a Bloomberg announcement of a new transaction (Deal Bloomberg) will be subject to a similar regulatory framework, but with slightly different outcomes. But unlike the Non-deal Bloomberg (where the "offer" of securities is sometimes in question), the Deal Bloomberg will most certainly constitute an offer of securities.

A Deal Bloomberg announcing a new transaction may comply with Rule 134 and, as a result, not be deemed a prospectus and, thus, be exempt from the SEC restrictions applicable to written offers. However, as mentioned above, many practitioners no longer believe that strict compliance with Rule 134 is necessary.

For the Deal Bloomberg, there should be little debate over the form of Rule 433 legend to be included. The names of the active book-running managers and their contact numbers will be included in the legend. And the exemption from filing provided by Rule 433(d)(5)(i) should apply to the Deal Bloomberg, given that it will likely not "reflect the final terms" of the securities. Also, as mentioned above, any legending contained in the Deal Bloomberg should generally sync up with what is provided in any roadshow slides that will be used to market the transaction.

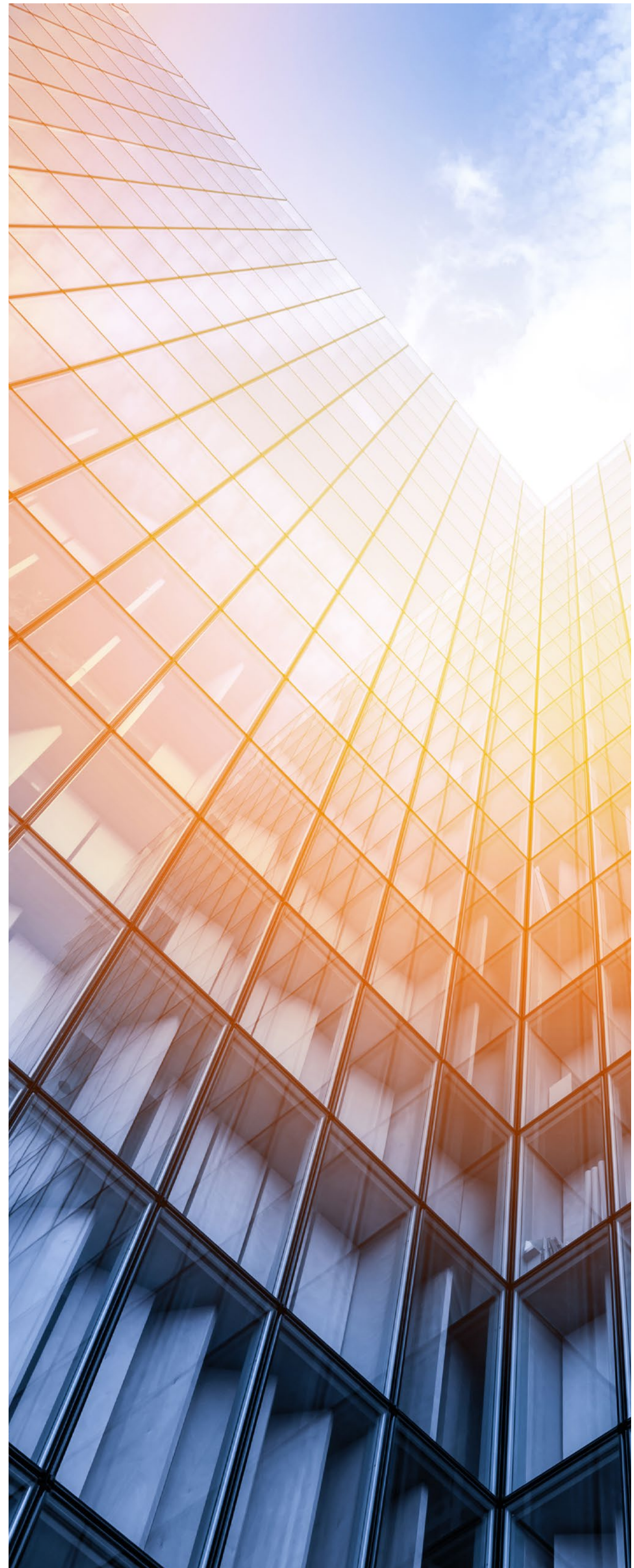
Principal Legal Framework

Section 11

For a registered offering, Section 11 of the 1933 Act imposes liability when a registration statement contains a material misstatement or omission.[2] If a Bloomberg Blast is considered an "offer of securities" and deemed to be a free writing prospectus subject to Rule 433, free writing prospectuses are not considered part of the registration statement. Therefore, the Bloomberg Blast should not be subject to Section 11 liability. This is an important distinction, as Section 11 imposes strict liability for any material misstatement or omission in the registration statement upon, among others, the issuer, its directors and the underwriters for the offering.

Section 12(a)(2) and Rule 10b-5

For a registered offering, a Bloomberg Blast that is considered an "offer securities" may be subject to liability under Section 12(a)(2) of the 1933 Act and Rule 10b-5 under the 1934 Act.



2 The specific language of Section 11 reads, "…an untrue statement of a material fact or omitted to state a material fact required to be stated therein or necessary to make the statements therein not misleading…"

Section 12(a)(2) provides the buyer of a security with a remedy for material misstatements or omissions[3] made by anyone who offers or sells the security by means of a prospectus (including a free writing prospectus) or an oral communication.

Rule 10b-5 under the 1934 Act deems it unlawful to employ any scheme or device to defraud, to make any material misstatements or omissions[4] or to engage in any acts or practices that would operate as a fraud or deceit on any person in connection with the purchase or sale of a security. In order to establish a claim under Rule 10b-5, an investor must prove that (1) there was a material misstatement or omission, (2) it was in connection with the purchase or sale of a security and (3) there was "scienter"—defined as the intent or knowledge of manipulation or deception.

Although a Bloomberg Blast could give rise to liability under Rule 10b-5 and Section 12(a)(2), its relatively brief disclosure should help to mitigate some liability risk. Other than credit ratings (which may or may not appear), the subject matter of Bloomberg Blasts are usually either verifiable facts or boilerplate. Furthermore, to the extent a 10b-5 claim was ever asserted with respect to Bloomberg Blast disclosure, the scienter element of a 10b-5 claim would seemingly be difficult to establish given the nature of the disclosure in a Bloomberg Blast.

Bloomberg Blasts, however, are typically not "scheduled out" in an underwriting agreement such that they are picked up in indemnity provisions. To the extent, then, that the Bloomberg Blast is an offer of securities but limited to a Rule 134-compliant announcement, it is unlikely that the underwriting agreement for the offering will provide indemnity for liabilities arising from the Bloomberg Blast.

If, however, the Non-Deal Bloomberg or Deal Bloomberg constitutes an "issuer free writing prospectus", as defined in Rule 433(h), the analysis may be different. The "free writing prospectus" will still not be part of the registration statement for the offering and therefore, not be subject to Section 11 liability under the 1933 Act. But, while practice varies, many underwriting agreements may provide indemnification if such a Bloomberg constitutes an "issuer free writing prospectus."

Conclusion

Despite the brevity of the typical Bloomberg Blast, the legal and practical considerations are nuanced. And market practice continues to evolve. But the announcements are central to the deal and the working group is well-advised not to give short shrift to its review and analysis.

3 The specific language of Section 12(a)(2) reads, "...an untrue statement of a material fact or omits to state a material fact necessary in order to make the statements, in the light of the circumstances under which they were made, not misleading..."

4 The specific language of Rule 10b-5 reads, "...any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading..."

Dark Company Debt: 15c2-11 Changes May Soon Be Coming

Introduction

Originally known as the "Penny Stock Quote Rule", Rule 15c2-11 (Rule) was adopted in 1971 to address fraudulent behavior in the over-the-counter (OTC) equity market. The Rule governs the publication or submission of quotations by broker-dealers in a quotation medium other than a national securities exchange. In general, the Rule provides that, before making known their interest in buying or selling an OTC security, broker-dealers are required to collect and review certain issuer information and confirm that such information is publicly available. Until recently, most practitioners believed that the rule applied only to OTC equity securities and not to OTC fixed income securities. However, in a September 2021 no-action letter, the SEC took a different position.

Requirements of the Rule

In 2020, the SEC adopted amendments to the Rule to promote investor protection by requiring improved public reporting of securities in the OTC market.[1] In the OTC market, broker-dealers facilitate access to OTC securities by serving as "gatekeepers" because, in the OTC market, retail investors own a predominant amount of OTC equity securities and publicly available information regarding OTC issuers often is limited.[2]

Specifically, the Rule requires broker-dealers to review basic issuer information prior to initiating or resuming quotations in an OTC security.[3] The broker-dealer must have a reasonable basis for believing this information is accurate and from a reliable source.[4]

The Rule includes three exceptions to the information review requirement for:

1. highly liquid securities of well-capitalized issuers (if the issuer satisfies a multi-prong test involving the security's worldwide average daily trading volume, the issuer's total assets and shareholders' equity);
2. underwritten offerings for securities by a broker-dealer that is an underwriter in the registration statement or offering statement; and
3. publicly available determinations by qualified interdealer quotation systems or a registered national securities association that the requirements of certain other exceptions are met.[5]

Broker-dealers may rely on quotations of other broker-dealers, as long as the initial broker-dealer complied with the information review requirement.[6] However, broker-dealers may only rely if there are no more than four business days in succession without a quotation.[7] This "piggy-back" exception requires the information to be current and publicly available (e.g. 10-K, 10-Q must be filed within 180 days of the end of the issuer's most recent fiscal year or quarterly reporting period.)

Notably, the SEC's final rulemaking in the 2020 amendments made only one mention of Rule 144A offerings, noting that the SEC believes exemptive relief from the increased demands of the Rule should be "narrowly tailored to limit access [to any 'gray' market outside of the Rule's purview] to sophisticated investors, such as qualified institutional buyers" pursuant to Rule 144A.[8]

1 Release No. 33-10842; 34-89891; File No. S7-14-19, 17 C.F.R. Parts 230 and 240, The Securities and Exchange Commission, September 16, 2020, *available at* https://www.sec.gov/rules/final/2020/33-10842.pdf, at 7.

2 *Id.* at 5.

3 *Id.* at 6. See also Rule 15c2-11(b) Specified Information. In particular, (b)(5) sets forth a list of items to be provided if certain other annual reports described in (b) are not available. And (b)(5) includes the following with respect to financial statements:
(L) The issuer's most recent balance sheet (as of a date less than 16 months before the publication or submission of the quotation) and profit and loss and retained earnings statements (for the 12 months preceding the date of the most recent balance sheet);

4 *Id.* at 7.

5 *Id.* at 9.

6 *Id.*

7 *Id.*

8 *Id.* at 77.

Phased-In Application of the Rule to OTC Fixed Income Securities

In the summer of 2021, to the surprise of many market participants, the staff of the SEC's Division of Trading and Markets signaled that the Rule applies to other types of OTC securities, including fixed income securities. In September 2021, the staff issued a no-action letter[9] to the Financial Industry Regulatory Authority, Inc. (FINRA) affirming the Rule's application to fixed income securities and providing broker-dealers with relief until January 23, 2022 to comply with the Rule's application to fixed income securities.

In December 2021, the SEC issued a second no-action letter to FINRA (the December No-Action Letter) which again confirmed that the SEC was changing its course with respect to a long-standing interpretive rule by applying the Rule to OTC fixed-income securities, including high-yield debt securities issued for resale under Rule 144A.[10] Additionally, the December No-Action Letter established the following phase-in periods for the Rule's applicability to fixed income securities:[11]

1. Phase I: From January 3, 2022 to January 3, 2023, the Rule will apply to fixed income securities or issuers meeting certain criteria where there is current and publicly available financial information about the issuer (e.g., (1) has a class of securities listed on a national securities exchange or (2) is subject to the reporting requirements of the 1934 Act and current in such reports); provided, however, that this first phase also exempts OTC fixed income securities offered pursuant to Rule 144A.[12]
2. Phase II: From January 4, 2023 to January 4, 2024, the Rule will apply to the same categories as Phase I, but there is no exemption for fixed income securities offered pursuant to Rule 144A.
3. Phase III: After January 5, 2024, the Rule will apply to the same categories as Phase II and also either (1) the fixed income security is foreign sovereign debt or a debt security guaranteed by a foreign government or (2) there is a website link showing information compliant with the Rule, provided the broker-dealer has determined the website link is current on at least an annual basis.

Impact to Dark Company Rule 144A Offerings

Rule 144A provides a safe harbor from registration for resales of securities to qualified institutional buyers (QIBs). Rule 144A transactions are generally conducted with a disclosure document subject to 10b-5 antifraud protections under the 1934 Act. Additionally, indenture reporting obligations for a "private for life" debt instrument generally require that certain limited issuer information only be "available upon request", as required pursuant to Rule 144A(d)(4). To facilitate investor interest, issuers also often agree to covenants in the indenture to provide ongoing financial information through a password protected website. From a policy perspective, when adopting Rule 144A, the SEC concluded that the "available upon request" approach appropriately balanced investor protection and capital raising goals. Inherent to this balancing act was the sophisticated nature of the eligible 144A investors. Given this disclosure construct, companies that are not subject to 1934 Act reporting requirement (dark companies) have been frequent issuers in the 144A capital markets.

In contrast to the "available upon request" regime of Rule 144A, as of January 4, 2023, the Rule will require that, in order to publish quotations for 144A securities trading in OTC markets, broker-dealers review certain issuer information (the scope of which is generally consistent with the requirements of Rule 144A) and confirm such information is available to the public. Certain industry groups have noted that by requiring Rule 144A issuer information to be made

9 Securities and Exchange Commission, Letter to Financial Industry Regulatory Authority, Inc., dated September 24, 2021, "Re: Amended Rule 15c2-11 in Relation to Fixed Income Securities," *available at* https://www.sec.gov/files/rule-15c2-11-fixed-income-securities-092421.pdf.

10 Securities and Exchange Commission, Letter to Financial Industry Regulatory Authority, Inc., dated December 16, 2021, "Re: Amended Rule 15c2-11 in Relation to Fixed Income Securities," *available at* https://www.sec.gov/files/fixed-income-rule-15c2-11-nal-finra-121621.pdf.

11 December No-Action Letter at 2.

12 See Appendix A to December No-Action Letter. Among other qualifying items, the December No-Action Letter provides relief when: "The subject security is a fixed income security or asset-backed security offered pursuant to Rule 144A under the [1933] Act, and the broker or dealer reasonably believes that the issuer of the subject security will provide the information specified in Rule 144A(d)(4), prior to a Rule 144A transaction, upon request.

available to non-QIBs in the general public (which would include investors who are not eligible to invest in Rule 144A securities), the SEC staff is contradicting the "available upon request" concept and the underlying policies embodied in Rule 144A. This requirement is concerning for dark companies that are private and do not issue SEC-registered debt or have listed securities—and, thus, are not required to make public their financial statements.

To the extent the Rule applies to 144A fixed income securities on January 4, 2023, a wide swath of the 144A debt market will be impacted. For example, price quotations of certain 144A OTC debt securities may disappear because broker-dealers may not be permitted to publicly indicate their interest in buying/selling such debt if issuer information is not publicly available. This result could impact liquidity in existing 144A OTC debt. Further, to the extent liquidity in the 144A OTC market is diminished, debt costs could increase for dark companies looking to access the private debt capital markets.

SIFMA has been quite active and vocal in publicizing the seemingly contradictory policy goals of Rule 144A and the SEC's new interpretation of the Rule. Given the material impact of such changes on portions of the 144A market, SIFMA has requested the SEC to suspend implementation of the new interpretation of the Rule to the fixed income market. Further, SIFMA has requested the SEC to initiate a formal and public rulemaking process for the changes in the Rule to weigh the costs against the benefits. To date, however, the SEC has not backed away from the January 4, 2023 implementation date.

BASELOAD is prepared from time to time to provide general information about selected power and utilities capital markets developments and issues for attorneys at Hunton Andrews Kurth LLP, and is provided to clients and friends of Hunton Andrews Kurth LLP. It is not intended to provide legal advice or legal opinions and must not be relied on as such. If you have questions related to any of the articles in this issue, please contact any of the below members of the Power and Utilities Capital Markets group at Hunton Andrews Kurth LLP:

Joseph B. Buonanno
Partner
+1 704 378 4750
jbuonanno@HuntonAK.com

Michelle Chan
Associate
+1 212 309 1350
mchan@HuntonAK.com

Monika Dziewa
Associate
+1 212 309 1377
mdziewa@HuntonAK.com

Michael F. Fitzpatrick, Jr.
Partner
+1 212 309 1071
mfitzpatrick@HuntonAK.com

Steven C. Friend
Partner
+1 212 309 1065
sfriend@HuntonAK.com

Brendan Harney
Associate
+1 212 309 1255
bharney@HuntonAK.com

Matthew Hayes
Associate
+1 212 309 1274
mhayes@HuntonAK.com

Patrick Jamieson
Associate
+1 212 309 1049
pjamieson@HuntonAK.com

Adam O'Brian
Partner
+1 212 309 1043
aobrian@HuntonAK.com

Peter K. O'Brien
Partner
+1 212 309 1024
pobrien@HuntonAK.com

Reuben H. Pearlman
Associate
+1 212 309 1109
rpearlman@HuntonAK.com

Thomas White
Associate
+1 212 309 1389
twhite@HuntonAK.com

Alice Yao
Associate
+1 212 309 1376
ayao@HuntonAK.com

HUNTON
ANDREWS KURTH

© 2022 Hunton Andrews Kurth LLP. Attorney advertising materials. Hunton Andrews Kurth, the Hunton Andrews Kurth logo, HuntonAK and the HuntonAK logo are service marks of Hunton Andrews Kurth LLP. These materials have been prepared for informational purposes only and are not legal advice. This information is not intended to create (and receipt of it does not constitute) an attorney-client or similar relationship. Please do not send us confidential information. Past successes cannot be an assurance of future success. Whether you need legal services and which lawyer you select are important decisions that should not be based solely upon these materials. Photographs are for dramatization purposes only and may include models. Likenesses do not necessarily imply current client, partnership or employee status. Hunton Andrews Kurth LLP is a Virginia limited liability partnership. Contact: Walfrido J. Martinez, Managing Partner, Hunton Andrews Kurth LLP, 2200 Pennsylvania Avenue, NW, Washington, DC, 202.955.1500

22653-1022