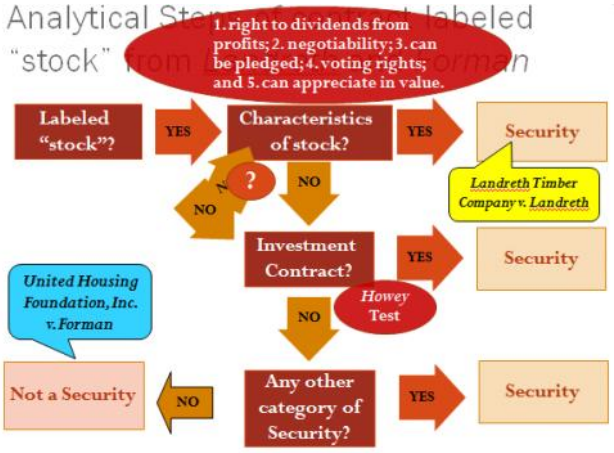
Is it a Security Approach

Thursday, December 01, 2011
12:01 PM

Is the instrument a security?
A security is an instrument enumerated in 2(a)(1) of the Securities Act which includes stocks, notes, and investment contracts. Whether an instrument is a "security" really is the question of whether that instrument should be regulated by the securities laws.

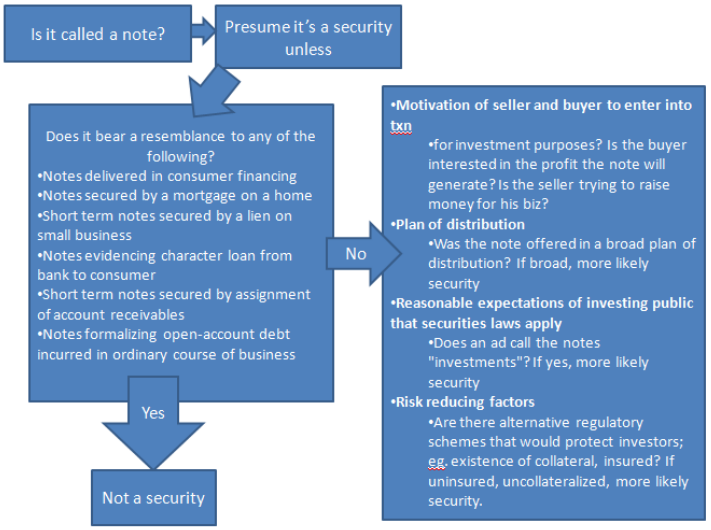
a. **Is it found in the Statutory List under Section 2(a)(1)?**
   i. **Instruments known as securities** (e.g., stocks, bonds)
      1) **Stocks**
         a) Is it labeled stock?
            i) If yes, then, considering investor expectations, people purchasing may have (1) thought they would be protected by the securities laws and (2) would have otherwise invested in real stock in the capital markets.
         b) Does it have the characteristics of stock? 4 characteristics of common stock set forth in Forman:
            i) **Voting rights** (in proprtn to shares owned) for bd. members, mergers, sales of assets, etc.
            ii) **Right to Dividends contingent on profits**
            iii) **Transferability** (can sell it to make money; negotiable; can be pledged as collateral)
            iv) **Possibility to appreciate in value**
         c) If the instrument embodies all of the above characteristics, it is stock, and it is a security.
         d) If not, go on to see if it qualifies as an investment K, or some other category of security.



      2) **Notes**
         a) Notes may be securities if they are issued for investment purposes. Commonly, notes have (1) fixed and periodic interest rate; (2) principal amount given by lender and then returned by debtor; (3) a maturity date for when the principal amount must be returned to lender.
         b) Is the note a security? **Reves**
            i) **Is the note called a note?**
               i) Take into account investing expectations
            ii) **Presume the note is a security, unless**
            iii) **It bears some resemblance to the following non-security notes**:
               i) Notes delivered in consumer financing
               ii) Notes secured by a mortgage on a home
               iii) Short term notes secured by a lien on small business
               iv) Notes evidencing character loan from bank to consumer
               v) Short term notes secured by assignment of account receivables
               vi) Notes formalizing open-account debt incurred in ordinary course of business
               vii) [consumer financing and commercial loans]
            iv) If it doesn't bear a resemblance to any of those, apply the following factors:
               i) **Motivation of seller and buyer to enter into txn**
                  a) Did they transact for investment purposes? Is the buyer interested in the profit the note will generate? Is the seller trying to raise money for his biz?
                  b) "if the seller's purpose is to raise money for the general use of a business enterprise or to finance substantial investments and the buyer is interested primarily in the profit the note is expected to generate, the instrument is likely a security"
                  c) On the other hand, if the note is exchanged to promote some commercial or consumer purpose, it is less likely to be a security.
               ii) **Plan of distribution**
                  a) Was the note offered in a broad plan of distribution? If broad, more likely security
                  b) "If there exists common trading for speculation or investment, the note is more likely a security. To establish that kind of trading, it must be shown that the notes were offered and sold to a broad segment of the public. "

iii) **Reasonable expectations of investing public that securities laws apply**
   a) Does an ad call the notes "investments"? If yes, more likely security
   b) "where, for eg, the notes are advertised as "investments" and no countervailing factors would lead a reasonable person to doubt this characterization, a security may be recognized. Accordingly, the court will consider instruments to be securities on the basis of such public expectations, even where an economic analysis of the particular transaction might suggest that the instruments are not securities as use din that transaction"

iv) **Risk reducing factors**
   a) Are there alternative regulatory schemes that would protect investors; eg. existence of collateral, insured? If uninsured, uncollateralized, more likely security.
   b) If there is another regulatory framework significantly reducing risk, no need to recognize the instrument as a security.



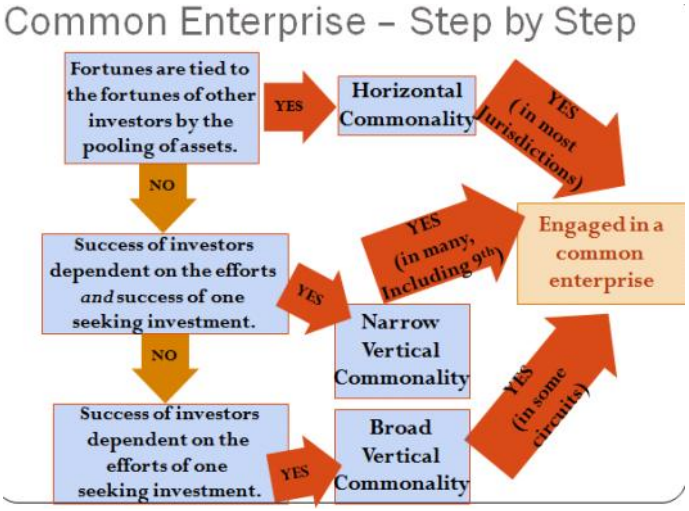
ii. Specific instruments (e.g., fractional oil interest, voting-trust certificate, certificate of deposit of a security, treasury stock, collateral-trust certificate, etc.)

b. **Investment Contracts (Howey test)**

An instrument is an investment K, and hence a security, when (1) investors invest money; (2) are dependent on other investors and/or the promoter for a return on their investment; (3) the interest is bought in order to obtain a financial return; and (4) investors don't participate meaningfully in the venture but instead rely solely on the efforts of others.

i. **A person invests his money**
   1) Invest money, cash?
   2) If not money, must be something of value
      a) Should be something that would have otherwise gone to the capital markets
      b) Eg. Labor is valuable but usually the person is only contributing labor to make a livelihood; only qualify if it would have been invested elsewhere
   3) Investing should be voluntary/free choice (**Daniels** - pension plan case)
      a) Intent to invest, link to capital markets

ii. **In a common enterprise** (**SG Ltd** - virtual stock exch case)
   1) Circuits differ as to whether one or both horiz and vert. are needed
   2) Horizontal commonality
      a) Pooling of investor assets?
      b) All investors share in same risks/profits of enterprise
         i) Rationale - collective action problem; common info desired
   3) Broad vertical commonality
      a) Investor returns/success loosely depend on the effort, expertise of the promoter
   4) Strict vertical commonality
      a) Investor returns/success loosely depend on the effort, expertise of promoter & promoter has his own stake in the outcome
         i) Watch out for when the promoter gets paid a fixed fee



iii. **And is led to expect profits**
   1) Investor must be investing to try to get more money
   2) More than just consumption of the interest acquired (**Forman**)
   3) Types of profits:
      a) Capital appreciation resulting from the development of the initial investment
      b) Distributions of earnings resulting from the use of investors' funds (eg. Dividends) (**Forman**)
      c) Fixed returns (**Edwards** - lease buyback agreement)
   4) Can't be: tax deduction, favorable tax consequences, savings by having low rent.
      a) "investor seems to be motivated by a desire to obtain/consume ___, rather than seeking a return on the acquisition"

iv. **Solely from the efforts of others**
   1) Need not be 100% efforts of others
   2) Effort is on a sliding scale, consider:
      a) Investor involvement undermines policy rationales (if involved in biz, they don't have info asymmetry);
      b) c/a - involvement insignificant, still no access to info.
      c) c/c/a - the investor is sophisticated, or has bargaining power, so whether involved or not, securities laws need not mandate disclosure here
   3) Watch out for referral fees
   4) Watch out for the enterprise's success being tied to pure luck
      a) Consider: what kind of info would the investor need to assess for the investment now and going forward? If that info is the type that the promoter can disclose cheaply, and the investors don't have access to it, more willing to find a "security" and regulate this txn.
   5) **Partnerships**
      a) General partnership interest is not considered a security because general partners usually [and by definition/ matter of law] take active role in the partnership.
         i) General partnership interest is considered a security when the general partner retains little ability to control or manage the profitability of the investment:
            i) **Agreement leaves little power in hands of investor-partner**
               a) Or the power was illusory (per Merchant Capital)
            ii) **Investor-partner lacks experience and knowledge in business affairs of that enterprise as to be incapable of intelligently exercising his or her partnership powers**
               a) Look at that particular enterprise
            iii) **Investor-partner is so dependent on a unique entrepreneurial or managerial ability of the manager that he cannot in all practicality replace the manager or otherwise exercise meaningful partnership powers**
               a) Eg. Money is so tied up in a contract that the manager/promoter negotiated and only he can touch it
      b) Limited partnership interest is generally considered a security when the limited partner is **passive and relies on the general partners to manage the enterprise**.
         i) Limited partnership interest is not a security if the limited partner has explicit voting power on, eg. Whether specific pieces of land should be sold; if retains pervasive control over its investment such that it cannot be deemed a passive investor. (ie. limited partners can engage in extensive activities yet retain their limited liability status)
      c) Limited liability partnership interest is generally considered a security because, by their definition, they are registered with the state and partners in the LLP are NOT vicariously liable for the LLP's debts and obligations; hence partners tend to be extra-passive because no incentive to retain control over biz.

v. Land+Services contracts may be securities when there's a offer/sale of some land coupled with the promoter performing certain rental services for the purchaser-investor. À la **Howey**
   1) Make sure the investor is buying into the agreement for investment purposes, not to buy a condo, find a job, make a living.
   2) Also, land + services K will normally not satisfy the horizontal commonality prong (unless there's a pooling of investor money to build condos/strip malls and distribute profits pro rata).

vi. Franchise agreements (or dealerships, distributorships, leasing arrangements) are typically not investment Ks because of the meaningful managerial efforts the franchisee-investor puts in (eg. The day to day operations, maintaining the store, paying costs of operation, keeping employee rationale).

1) A franchise is an investment K where the franchisee-investor doesn't have any meaningful or realistic authority over the franchise. (like not even any power over the day-to-day operations)
2) But if the franchise agreement is really a **pyramid scheme** (where profits are sought from selling more and more franchises (by recruiting more and more franchisees)) then an investment K will normally be found.

c. **Are there alternative federal regimes that preclude securities regulation? (Daniels, Marine Bank)**
   i. Does the FDIC insure the certificates of deposit?
   ii. Is the mandatory pension plan regulated by ERISA?

Gun Jumping Rules Approach

Monday, November 28, 2011
12:32 PM

Gun Jumping rules analysis

A. Are you in registration

a. In registration signifies the registration period where the issuer being talking with U/Ws up until the completion of the offering period.
b. Has the company taken preliminary steps for considering a PO?
c. Has the board decided to go public and began talking with i-banks?

B. **Who is doing what?**

a. Section 5 applies to issuers, U/Ws, dealers in public offering context
b. Section 5 does not apply to secondary market actors who aren't issuers, U/Ws, or dealers
c. Section 5 doesn't apply to unsolicited brokers' transactions
d. Doesn't apply to transactions by a dealer outside of the 40-day period after the reg. stmt effective

C. **Is there a registration statement?**

a. Filed? In effect?

D. **Pre-Filing**

a. During the pre-filing period, **5(a)** bans sales until the reg. stmt effective and **5(c)** bans all offers before the filing of the reg. stmt.
b. Per **2(a)(3)**, an offer is broadly defined as any offer or any attempt to dispose of or solicit an offer to buy a security. [this definition excludes such communications as between the issuer [or anyone controlling or controlled by the issuer], U/W, or amongst U/Ws.]
c. Further, efforts that **condition the public mind** or arouse public interest in particular securities constitute an offer.
d. Does it condition the public mind? Consider the following factors:
    i. **Motivation of the communication.** Was the statement made for the purpose of peaking interest in the PO? Was the statement made before there was any PO decision?
    ii. **Type of info communicated.** Is it soft (forward looking, hard to verify, more like an offer) or is it hard (factual, financials, proxy statements, dividend notices, financial development to the press,[commercial communications] less like an offer)?
    iii. **Breadth of the distribution**. Was the communication broadly disseminated, looking more like conditioning the public? Or was it narrow, to select group?
    iv. **Form of the communication.** Was it a written or recorded communication that is easily reproducible, looking more like conditioning the public? Or just a spoken statement that could not be reproduced?
    v. **Are particular facts about the offering mentioned?** Was the U/W mentioned, or mentioned by name? Is the type of security, the amount, the price mentioned? If yes, then it's very likely conditioning the public mind and very likely an offer because there would be no other purpose for such a communication than to type the upcoming offering.

e. **Does a safe harbor, making it otherwise not an "offer", apply?**
    i. **135**
        1) Short, factual notices though any medium announcing a proposed registered offering by the issuer is not an 'offer' if (1) the ad contains a legend clarifying that the ad is not an offer; (2) the info is limited to (a) the name of the issuer; (b) title, amount, and basic terms of the securities; (c) the amount of the offering; (d) the anticipated timing of the offering; (e) a 'brief statement' of the manner and purpose of the offering, without naming the U/Ws; (f) whether the issuer is directing its offering only to a particular class of purchasers. Any other information contained in the Ad will be considered an "offer." (3) U/Ws cannot use this SH.
        2) Can't name the U/Ws or that there are U/Ws in the offering
        3) The issuer may reference the offering in this SH.
        4) No forward-looking statements allowed

    ii. **163**
        1) Communications by **WKSIs** in the pre-filing period are not "offers" for 5(c) purposes provided that (1) the issuer is a WKSI (defined in Rule 405); (2) the communication is deemed an FWP and a prospectus under 2(a)(10); (3) if it's a **written** communication, there is a **legend** as provided by 163(b)(1)(i) [saying the issuer will file a reg stmt and you should read that and the prospectus, available on SEC website] (**immaterial** failure to include the legend is ok so long as there was good faith/reasonable effort to comply with the legend condition, the FWP is amended to incl the legend ad soon as practicable); (4) the communication is filed upon filing of the reg stmt;
        2) U/Ws cannot use this SH.
        3) They can reference the offering
        4) A WKSI pre-filing statement made under this rule would still be considered a "prospectus" for 12(a)(2) purposes

    iii. **163A**
        1) Statements made prior to the **30 day period** before the filing of the registration statement are not offers under 5(c) as long as (1) they were made by or on behalf of the issuer, (2) they do not refer to the offering, (3) the issuer takes reasonable steps to prevent dissemination of the communication during that 30-day pre-filing period, and (4) U/W can't use this SH.
        2) Cannot refer to the offering
        3) All issuers can use this SH.

iv. **168**
1) **Reporting Issuers** communicating factual business info and forward looking info regularly released in the ordinary course of business in same type/manner are not an "offer" if: (1) the issuer is a reporting issuer; (2) it is factual business info as defined in 168(b)(1) or forward-looking info as defined in 168(b)(2); (3) the issuer has previously released or disseminated the info of the type; (4) the type, manner, and form of the info released now is consistent with the past releases; and (5) the communication **does not mention the offering**.
2) Factual biz info:
1) Factual information about issuer, its business or financial developments, or other aspects of its business;
2) Advertisements of, or other info about, products, services; …
3) Forward-looking info:
1) projections of revenues, income (loss), earnings (loss) per share, dividends, capital structure, etc.;
2) statements about management's plans for future operations, including plans about products and services
3) Statements about the issuer's future economic performance, including statements of the type contemplated by the management's discussion and analysis of financial condition and results (MD&A type info); and
4) Assumptions underlying or relating to any of the info described above.

v. **169**
1) **Non-Reporting Issuers** communicating factual business info regularly released in the ordinary course of business in the same type/manner are not "offers" if: (1) non-reporting issuer; (2) it is factual business info as defined in 169(b)(1); (3) the issuer previously released or disseminated the information in the ordinary course of business; (4) does not apply to communications made by U/Ws; (5) cannot refer to the offering; (6) the type, manner, and form of the info released now is consistent with the past releases; (7) the information cannot be directed to investors or potential **investors in their capacity as such** (has to be communicated for intended use by customers and suppliers) (even if it's been sent out before in ord. course).
2) No forward looking stmts
3) No U/Ws

vi. If the communication doesn't fit in any of these safe harbors, it doesn't mean it's an offer --- you can still argue that it's not an "offer" by using the factors (motivation of commctn, type of info, breadth of distribution, form of communication, don't mention any specifics about the offering)

E. **Waiting Period**
a. In the waiting period, 5(c)'s ban on offers no longer applies, but 5(a) and 5(b)(1) apply.
b. 5(b)(1) prohibits the transmission of a prospectus that does not comply with Section 10 requirements.

c. **Is it a prospectus?**
i. A prospectus, per 2(a)(10) is defined as any written or broadcast communication offering a security.
ii. **Is it written or broadcast?**
1) Oral communications are not prospectuses.
2) Road shows are considered oral communications and offers, and are not prospectuses under 2(a)(10).
iii. **Is it an offer?**
1) Per 2(a)(3), an offer is broadly defined as any offer or any attempt to dispose of or solicit an offer to buy a security.
2) Further, efforts to condition the public mind or arouse public interest in particular securities constitute an offer.
3) Factors: motivation; type of info; breadth of distribution; form of communication; facts about the offering.
4) Safe Harbors? 135, 163, 163A, 168, 169

iv. **If it's a written offer, is it otherwise not a "prospectus"? 2(a)(10)(b); Rule 134; Roadshows**
1) **Tomstone Ads**
1) **Tombstone ads under 2(a)(10)(b)** are exempt from the definition of prospectus. These are written communications that state where a written section 10 prospectus can be obtained, plus brief information about the security, the price, and where you can make an order.
2) Under **Rule 134**, After a registration statement has been filed, written communications that provide no m ifore information that that listed in the rule are not "prospectuses": (1) it contains no more info that that listed in 134(a)(1)-(22); (2) if required, it contains a legend as per 134(b)(1) that the reg stmt has been filed but its not effective, so the securities cannot be sold or purchased AND states the name and address of a person from whom a written section 10 prospectus may be obtained; (4) **but legend not required** but CAN be contained in communications which do no more than state from whom a written prospectus can be obtained and include a URL where the prosp may be obtained; (5) legend not required but CAN be contained in communications that already are preceded or accompanied by a section 10 prospectus (prelim. Prospectus OK - anything other than an FWP). (6) A communication sent under this SH that is also accompanied or preceded by a section 10 prospectus MAY SOLICIT an offer to buy the security or request that the recipient indicate whether he might be interested **so long as it contains a disclaimer-like legend**. (7) When the rule requires the communication to accompany/be preceded by a section 10 prospectus, and the actual communication is electronic, providing a hyperlink to the prospectus is fine.
3) Forward-looking info NOT OK
4) "three years of audited income statements, including revenues, costs, earnings" is NOT OK
5) U/Ws can use this
6) OK Ads under this rule:
Three types of Ads under this rule:

1. Advertisement of offering with lots of shit about the offering and the company + a legend.
2. Advertisement of offering with lots of shit about the offering and the company + Rule 430 prospectus
    i. No legend needed but you can throw one in there
    ii. 134(d) This communication may solicit from recipient an offer to buy; may also request the recipient indicate his interest somehow. But it has to have a disclaimer: no offers to buy can be accepted until the reg. stmt. has become effective.
3. Advertisement that only says, where you can obtain a prospectus, and provide the link. Can also say what type of security, the price, and where/who you can make orders. (oldschool tombstone ad)
    i. No legend needed but you can throw one in there.

1) **If there's a prelim prospectus + tombstone ad that names U/Ws and their roles, no legend + mail back card ==> OK**

2) **Road Shows**
    1) **Road shows** are not "prospectuses" under the meaning of 2(a)(10) as they are oral communications and offers. Under Rule 433(d)(8), written materials used in road shows and only available as part of the road show are also not considered prospectuses.
    2) But recorded road shows (non-live recorded) is a prospectus, but the issuer doesn't have to file it with the SEC. But a non-reporting issuer must file an electronic road show unless they make a copy of one available online
        i) If the written communications are available outside the road show (posted online, passed out), then they are considered FWPs and must be filed pursuant to Rule 433.
3) Oral Solicitations
    1) Non-broadcast oral statements are expressly allowed under 2(a)(10)'s definition of prospectus.
    2) In the waiting period, a broker of issuer-co finds out about the upcoming IPO, so she calls up a bunch of her favorite college friends and tells them issuer is awesome, their stock will rise if you buy.
    3) This is ok under 5(b)(1)
    4) Might have a 10b-5 problem

v. **If it's a prospectus, does it comply with section 10? 10(a); Rule 430, Rules 164 & 433 FWP meet 10(b)**
1) Three options: 10(a) prospectus; preliminary prospectus under Rule 430; FWP under Rule 433 and 164.
2) **10(a)**
    1) 10(a) prospectus contains everything in the registration statement, minus some of the documents.
3) **Rule 430 Preliminary Prospectus ("red herring")**
    1) Under **Rule 430**, a prospectus meets requirements of §10 for purposes of §5(b)(1) if, prior to effective date, the statement contains substantially the same info required by 10(a) but omits info wrt the offering price, the U/W discounts or commissions, discounts or commissions to dealers, amount of proceeds, conversion rates, call prices, or other matters depending on price. A Rule 430 prospectus must contain a legend in red ink stating that a registration statement has not yet become effective. It must also contain a form of Statement of Add'l Information available upon request. If all the requirements of Rule 430 are met, issuers may freely these out to potential investors.
4) **Rules 164 and 433 FWPs**
    1) Under **Rule 164**, an FWP is a written communication (any communication that's not oral or live) that offers to sell/solicits an offer to buy a security that doesn't meet the requirements of section 10. If it complies with conditions set out in Rule 433, it satisfies 10(b).

    2) (1) Must have filed a **registration statement**;
    3) (2) **433(b)(1)-(2),** if **non-reporting**, unseasoned issuer, must also accompany/precede every FWP with a section 10 prospectus (can use Rule 430 prospectus during waiting period; hyperlinking is fine)
        i) but if you already sent out an FWP with the accompaniment, no need to send another section 10 prospectus with your FWP unless the prospectus has changed;
    4) (3**) 433(c),** FWP can contain **info** not contained in reg stmt so long as it doesn't conflict with info contained in reg. stmt or periodic reports;
    5) (4) **433(c),** must contain a **legend** per Rule 433(c)(2)(i)-(ii) saying the issuer has filed a reg stmt but you should read the prospectus before you invest AND here is the email address where add'l documents can be requested;
    6) (5) **433(d)(1)(i), Issuer must file**, by date of first use: (a) FWPs that are distributed, prepared, used by the issuer ("issuer free writing prospectus") and (b) any portions of FWPs created by offering participants that contain issuer information.
        i) 433(d)(1)(i)(B) - **Issuer need not file participant FWPs that contain info only "derived" from issuer info. Eg. Information that is prepared on the basis of issuer information but doesn't directly contain the issuer info is not "issuer info" -- eg. U/Ws own valuation analysis**
        ii) (5.5) **433(f),** If the issuer or offering participant authorizes or provides any information that is later published by an unaffiliated **media source** eg. magazine, newspaper, etc., the conditions in (b)(2) and (c) do not apply, but the issuer or offering participant (a) must not have paid the media source, and (b) must file the communication and include the 433(c)(2) legend within 4 business days of becoming aware of its dissemination (unless it's already been filed).
    7) (6) **433(d)(1)(ii), offering participant must file** FWP by date of first use if it was reasonably designed to achieve broad unrestricted dissemination
        i) eg. Send out a press release; give copy of packet to a NYT journalist;
        ii) BUT NOT: U/W sends FWP to list of clients and customers (SEC Release No. 8501),
    8) (7) **433(d)(3)-(4),** however, there is no filing requirement for issuers/participants for that FWP if it was already

previously filed w/ the SEC and there are no material changes or additions. (8) there is also no filing requirement for issuers if previously-filed FWPs contain the issuer information.

9) (9) **433(g),** Issuers and participants must retain all FWPs they have used (unfiled) for 3 years following the initial bona fide offering of the securities.
10) (10)**164(b),(c),(d),** if there was an **innocent mistake** regarding whether to file, include legend, or retain, under Rule 164(b), the issuers/participants can cure "immaterial" failures if they acted in (a) good faith and with (b) reasonable care and (c) remedy the problem.

vi. **If the communication is a valid 10(a) prospectus, preliminary prospectus, or FWP, then it meets section 10 and doesn't violate 5(b)(1).**

F. **Post Effective Period**

a. The 5(b)(1) ban on carrying a prospectus that doesn't comply with section 10 still applies in the post effective period. 5(b) (2) also mandates that the delivery of securities must be accompanied with a 10(a) prospectus.

b. 5(b)(1) Analysis - Same exact as above

i. **Is it a prospectus?**
i. A prospectus, per 2(a)(10) is defined as any written or broadcast communication offering a security.
ii. **Is it written or broadcast?**
1) Oral communications are not prospectuses.
2) Road shows are considered oral communications and offers, and are not prospectuses under 2(a)(10).
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3) Factors: motivation; type of info; breadth of distribution; form of communication; facts about the offering.
4) Safe Harbors? 135, 163, 163A, 168, 169

iv. **If it's a written offer, is it otherwise not a "prospectus"?**
1) **Tombstone Ads**
1) **Tombstone ads under 2(a)(10)(b)**
2) Under **Rule 134**
2) **Road Shows**
1) Road shows are not "prospectuses"
3) **Traditional free writing**
1) **2(a)(10)(a).** Post effective, a communication isn't a "prospectus" anymore if a section 10(a) prospectus was sent (now or previously) to the person who received the current communication.

ii. **If it's a prospectus, does it comply with section 10 requirements?**
i. 10(a)
ii. FWP under Rules 164 and 433
1) Can no longer use a Rule 430 preliminary prospectus to accompany the FWP

c. 5(b)(2) Analysis

i. 5(b)(2) mandates that the delivery of securities must be accompanied with a 10(a) prospectus.
i. This is achieved via 5(b)(1) because a written confirmation of sales is a prospectus under 2(a)(10), and if accompanied by a 10(a) prospectus, it constitutes traditional free writing and does not invoke section 5(b)(1).

ii. Is there a delivery requirement to ____? The prospectus delivery requirement under 5(b)(2) applies to everyone except those outlined in section 4 and Rule 174.
[who is the person and indicate which exemption applies to him]
i. 4(1) exempts anyone who is not an issuer, U/W, or dealer from this delivery requirement.
ii. 4(3) exempts dealers and U/Ws who are acting as dealers (no longer acting as U/Ws for the offering), unless (a) the transaction takes place during the 40 day period after the effective date of the reg. stmt or; (b) if the securities of the issuer have never been sold (it's a true IPO), then the applicable period is 90 days; and (c) **4(3)(c),** if the transaction is for an U/W's unsold allotment, the U/W has a forever delivery requirement.
1) Under 174(b), there is no prospectus delivery requirement for dealers and U/Ws acting as dealers as to reporting companies. 174(d) states that if (1) it's a non-reporting issuer but (2) as of the offering date, the security is listed on a registered national securities exchange, then the delivery period is 25 days. 174(h) also says that any obligation under Rule 174 or 4(3) to deliver a prospectus can be satisfied by Rule 172's access equals delivery.
iii. 4(4) exempts brokers when executing unsolicited broker's transactions .

iii. Was Delivery Sufficient?
i. The 5(b)(2) prospectus delivery requirement is satisfied if the conditions of Rule 172 are met. Among the requirements is that a registration stmt is effective and that the final statutory 10(a) prospectus is filed with the SEC.
ii. Under Rule 172, Issuers, U/Ws, dealers may choose not to send out the final 10(a) prospectus with the written confirmation of sales so long as (1) **a registration statement is filed** and (2) the 10(a) **prospectus is filed** with the SEC (or if not filed, issuer made a good faith and reasonable effort to file). Note the condition set forth in 172(c)(3) that a 10(a) prospectus must be filed need not be met for a **dealer** to benefit from this safe harbor.

iii. If the conditions in Rule 172 are met, it exempts written confirmations of sales from the reach of 5(b)(1), AND 5(b)(2) is met.

iv. Did ____ Satisfy the Notice Requirement?
   i. **Rule 173** has a notice requirement that is tied to the prospectus delivery periods. If there's a prospectus delivery requirement, an U/W/dealer/issuer has to provide either a 10(a) prospectus or a notice saying that one would be required if it weren't for Rule 172 **within 2 days of completion of the sale**. This is to notify purchasers of legal rights under sections 11 and 12.
   ii. This notice requirement applies even if the U/W/dealer/issuer relies on Rule 172 to effect delivery; would still have to send them a little notice w/in two days following completion of the sale that they would have been entitled to receive a 10(a) prospectus.

v. The Delivery Periods Still Matter in Other Contexts:
   i. Rule 172 only applies to written confirmations of sales and notices of allotment of securities. Apart from those two things, the prospectus delivery requirement time periods are still crucial for: (1) free writing under 2(a)(10)(a) that require actual delivery of a 10(a) prospectus to satisfy 5(b)(1) **[does there need to a prospectus delivery requirement to still send the traditional free writing w/ a 10(a) prospectus?]**;
      1) At start of the post-effective period, an IPO issuer mails out a glossy brochure on the offering to drum up interest among investors.
         1) This is a prospectus and unless it's accompanied by a 10(a) prospectus (because it's an unseasoned/non reporting issuer) and make it an FWP, it will violate 5(b)(1).
         2) 172 won't work because 172 only exempts confirmations of sales and notices of allocations.
   ii. (2) **Rule 173** has a notice requirement tied to the prospectus delivery periods-- if there's a prospectus delivery requirement, an U/W or dealer has to provide either a 10(a) prospectus or a notice saying that one would be required if it weren't for Rule 172 within 2 days of completion of the sale.

Civil Liability Approaches

Monday, November 28, 2011
10:18 PM

a. **Section 11**
   1. Section 11 governs fraud in the registration statement; it prohibits material misstatements, omissions of material facts that must have been stated, and omissions to state a fact that is necessary to make a statement not misleading at the time the registration statement becomes effective.
   2. Show connection to interstate commerce
      i) Plaintiff must have purchased or acquired the security through a means or instrumentality of ISC.
   3. Action must be brought within section 13's statute of limitations, no later than 1 year after discovery of the falsity, and no later than 3 years after the security was bona fide offered to the public.
   4. Plaintiff must show tracing for standing
      i) There is a strict tracing requirement under section 11(a). Plaintiff must prove that (1) he or she acquired such security from the issuer in the PO or (2) he can trace the securities to the allegedly false reg. stmt. (Krim)
   5. Defendant must be enumerated in statute
      i) every person who signed the registration statement (6(a)) –includes issuer, CEO, CFO, comptroller or principal accounting officer, and the majority of its board
      ii) directors
      iii) experts (for their part)
      iv) underwriters
      v) And their controlling persons (Section 15)
   6. Plaintiff must prove
      i) Untrue statement of material fact;
      ii) Omitted to state a material fact required to be stated therein; or
      iii) Omitted to state a material fact necessary to make the statements therein not misleading
      iv) Materiality
         i) Material is when reasonable investor would think the fact would significantly alter the total mix of information . This is measured as of the time the registration statement became effective
         ii) Two ways to measure: measure magnitude via some metric; look at stock price change at disclosure of truth.
            a) When considering the magnitude, one popular rule of thumb is to look at whether the stmt relates to 5% of earnings, revenues, or income. If it relates to more than 5% of earnings, revenue, income, then it's likely material. Then, you have to consider qualitative factors to put the #s into perspective. "that particular misstatement allowed the company to meet expectations/mask a change in earnings. "
            b) When looking at stock price, (1) when was the truth really revealed into the mkt? on one hand, this could be the date.. On the other hand, this could be the date. (2) did the stock price change?
         iii) **11(a).** If the misstatement or omission was not material because (1) the market already knew about the fraud at the time of purchase, (2) was insignificant, then the misrepresentation is not actionable

   7. Plaintiff must not have known about the falsity
      i) **11(a).** If plaintiff knew about the misstatement/omission at time he/she purchased the securities, the fraud is not "material" and hence not actionable
   8. No intent requirement
      i) Defendant proves due diligence to avoid liability
         i) **Non-experts** as to non-expertised portions must prove (1) reasonable investigation; (2) reasonable ground to believe (3) did believe (4) all the statements in the reg stmt were true.
         ii) **Experts** may be liable only for those parts prepared or certified by them. An expert will never be liable as an expert for a non-expertise part of the reg stmt under §11(A)(4).
         iii) **Non-experts** as to expertised portions, only have to show (1) that they had reasonable ground to believe and (2) did believe that all the statements in the reg stmt were true.
         iv) **Experts** as to expertised portions, have to show that (1) after reas investigation, (2) he had reas ground to believe and (3) did believe (4) that the stmts in the reg. stmt. were true.
            a) Similar to what the non experts must prove for non expertised parts of the reg stmt.
         v) Reasonableness under 11(c) is that required of a "prudent man in the management of his own property." Under Rule 176, the reasonableness of investigation and of belief depends on various factors concerning the type of person and the nature of his relationship with the issuer.
      ii) Experts are: accountants, engineers, tax people, auditors.
         i) Attorneys rendering legal advice are NOT experts
      iii) Expertised portions: financials, audit statements
      iv) Non experts are executives, U/Ws, outside directors,
      v) Non expertised portions can be statement re the company, CEO's bio.
      vi) In the end, insiders/higher-ups will have a hard time proving due diligence because, given their position, it will be hard to believe they had reasonable grounds to believe a false statement was true.
         i) Insiders have access to lots of info; many of the insiders sign/guarantee the reg stmt
         ii) Outsiders don't have as much access but have duty to reasonably inquire and make independent verification of info; reasonably familiar with biz and operations? Regularly attend bd meetings where bd discusses every aspect of the biz? Familiar with co's development of new product lines? Involved in various co decisions?
   9. No need to prove reliance

i) unless P purchased after yr of earnings stmts generally available.

10. No loss causation requirement
    i) §11(e) permits the defendant to reduce (either in part or totally) the plaintiff's monetary recovery by showing that the loss (or portion thereof) was attributable to factors other than the material misrepresentations/omissions contained in the reg. stmt.

    ii) First, calculate the maximum amount of damages: IPO price - value of the security at time of suit, a la Beecher.
        i) The max amount of damages recoverable. Then D will argue, no, I am not liable for that entire amount. I am only liable for damages that my misstatement caused. So we have to look at the date of public disclosure and measure market reaction then.
    iii) Examine the date the public found out about the misstatement/the truth was revealed.
        i) P will argue the date on which the price dropped was the disclosure date
        ii) D will argue the date on which price went up was the disclosure date.
            a) Argue the facts for this -- eg. Disclosure to the SEC couldn't have been the operative date because that assumes insiders at the SEC leaked the information to the market.
            b) "the entire drop in price isn't caused by the misstatement because it wasn't until November the public knew about the misstatement, and if you want to see the effect of the misleading statement, look at how the price reacted on that November date."
    iv) If the court goes with the date where the price dropped, D will argue, yes, the price did drop, but it wasn't ALL due to the misstatement in the reg. stmt. The rest of the drop in price was due to overall market movement, other negative info in the news, etc.
            a) To make a compelling argument, D must present evidence that co behaved like other similar companies that went public at the same time and everyone did the same because of outside market factors. Must create a basket of stock and track how that basket did relative to your company.
        i) Pl. will rebut by saying the company's drop in price was in excess of the market, that the market knew of the misstatement like right after the IPO bc of a leak which caused this drop over a longer period, you disclosed positive info at the same time which offset the bad news.
            a) To make a compelling argument, P will say that the co underperformed the mkt (did worse than the mkt so there must have been some bad news) and plus, the companies you compared yourself to are very different, difft product, difft everything.

11. Damages are limited to the offering price
    i) Section 11(e) sets forth the calculation of damages to which a plaintiff is entitled. For each share traceable to the PO, §11 damages equal the difference between what the plaintiff paid for their shares (but not exceeding the offering price) minus one of three possibilities, depending on whether, and if so when, the plaintiff sold their shares. (1) if the plaintiff sold shares before suit, subtract price paid for shares by the resale price. (2) if the plaintiff still owns the shares at the end of suit, subtract the value of the shares at time of the filing of suit. (3) if the plaintiff sold the shares after filing suit but before judgment, then subtract the resale price (if it's greater than the value at the time of filing the suit). Per 11(g), the damages cannot exceed the price at which the security was offered to the public.
    ii) Underwriters cannot be held liable for more than the total price at which the securities underwritten by him were offered to the public.
    iii) When calculating the value of a security, price is only a good proxy for value at a given point in time if the market knew of all relevant and material info (and is efficient). Price will be a bad proxy for value if there is material information the market does not know, the market is irrational, or the market is inefficient.

12. Defenses
    i) Under **11(b)(1),(2)'s whistleblower defense**, if a nonissuer defendant discovers a material misstatement or omission in the registration statement and (1) resigns; and (2) tells the SEC about the alleged fraud then he is off the hook
    ii) **11(a).** If the misstatement or omission was not material because (1) the market already knew about the fraud at the time of purchase, (2) was insignificant, then the misrepresentation is not actionable
    iii) Under section 13's statute of limitations, section 11 lawsuits are barred after one year from the date plaintiff discovers the falsity, and the most, 3 years from the time of the offering.

13. Joint and Several Liability
    i) Under 11(a)(f)(1), violators generally are subject to joint and several liability, with two statutory exceptions. 11(e) limit s the liability of underwriters to the total price at which the securities underwritten by him and offered to the public. 11(f)(2)(A) limits the liability of outside directors to their proportionate liability (based on their degree of wrongdoing relati ve to that of other defendants).
    ii) Defendants can then seek to adjust their relative exposure to liability through both contract indemnification and contribution rights under section 11. as for contribution, in the trial of a non-settling D the jury assesses the relative culpability of everyone and only the non-settling Ds have to pay their share, the settling Ds need not pay another cent.

b. **Section 12(a)(1)**
1. Under section 12(a)(1), a person who offers or sells a security in violation of section 5 will be liable to the person purchasing such security from him for rescission, or if he no longer owns the securities, damages.

2. Must meet the SOL (no more than 1 yr from discovery of violation, no more than 3 yrs after offering)
3. Plaintiff is anyone purchasing a security from "seller" in violation of section 5
4. Defendants under 12(a)(1) include (1) actual sellers who pass title to the plaintiff and (2) people who successfully solicit the purchase, motivated by their own financial interest or that of the securities owner. Under section 15, (3) control persons of these defendants are also potentially liable unless they had (a) no knowledge of or (b) no reasonable ground to know about the facts giving rise to the liability here.

i) Examples
    i) Issuer as seller; dealer as seller; re-sale investor as seller; U/W as seller
    ii) Agent for a vendor (eg. Broker) who successfully solicits the purchase for the vendor can be a seller
ii) Can't sue seller's seller
iii) One statutory seller can sue another statutory seller for contribution.
    i) Eg. Issuer sells securities in a private placement; the selling agent F-s up. Violates section 5. E is an offeree, and he tells B about the offering. E just usually passes on tips like that to B.
        a) Issuer can only sue E for contribution as a statutory seller if E was himself soliciting for own/issuer's financial benefit.
    ii) Eg. Issuer wants to do a private placement, broker helps solicit people for the offering. Investor purchased directly from issuer. Sues issuer for violation of section 5 because they offered to someone who couldn't "fend for self." Issuer sues U/W for contribution.
iv) Control person can sue the statutory seller for contribution

5. Plaintiff must prove:
    i) Actual violation of section 5.
    ii) 12(a)(1) actionable section 5 violations
        i) Resale that isn't exempt from section 5
        ii) Selling before reg stmt effective w/o an exemption
        iii) Failure to deliver the prospectus when required to do so - 5(b)(2)
        iv) Made offer before reg stmt filed
        v) The section 5 violation does not need to be in relation to plaintiff's own purchase but the defendant-seller must have violated section 5 himself
            a) Bird purchased 100 shares in the IPO. Suppose issuer's U/Ws failed to send a final prospectus to Bird with her confirmation and the issuer also failed to file the final prospectus w/ the SEC.
            b) Rosita is another investor in the IPO. She did receive her final prospectus w/ her confirmation of sale. Can she bring suit under 12(a)(1) rescission for issuer's failure to send Bird a final prospectus with the confirmation of sale?
6. No real defenses
    i) Due diligence, good faith, reasonable care is irrelevant
    ii) No loss causation defense (issuer violates section 5 when selling to investor; market tanks because of shortage of lumber; investor can rescind the K for the purchase price he paid or, if already sold, get the purchase price - resale price)
    iii) Only real defense is to show the offering/txn qualified for an exemption to section 5
7. Damages
    i) Plaintiff is entitled to rescission or rescissionary damages. (1) If plaintiff still owns the security: purchase price - income received (dividends, etc); (2) If plaintiff already sold the security: purchase price - sales price - income received

c. **Section 12(a)(2)**

1. Under 12(a)(2), a person who purchased securities in a PO that was offered via a materially misleading prospectus can sue (1) the "seller"; (2) the solicitor of such security or (3) an issuer under Rule 159A when the plaintiff purchased from issuer in initial distribution for (1) rescission if still holds the security or (2) damages if sold the security. In order to have standing, there must have been a prospectus delivery requirement as to the plaintiff. There is a very loose reliance requirement.

a) Plaintiff must be a person who purchased securities acquired in a PO
b) Plaintiff must prove material misstatement/omission
    i) The misrep/omission must be in a prospectus or oral statement
    ii) "prospectus" is a document relating to a public offering
    iii) Docs involved in a private placement or a secondary market txn aren't covered by 12(a)(2) easy.
c) There must be a prospectus delivery requirement applicable to plaintiff
d) Plaintiff must not have known about its falsity
    i) D can use this as a defense
e) Defendants are those who offer/sell by means of the faulty prospectus
    i) Those who actually transfer title
    ii) Those who successfully solicit w/ motivation of own/securities owner's financial interest
    iii) Under 159A, can sue the issuer when plaintiff/purchaser purchased in initial offering w/firm commitment underwriting
    iv) Any control person of the above
f) No reliance requirement
    i) The "by means of" language is quite broad, requires a loose showing of a causal connection between the prospectus and the purchasing decision
g) No intent requirement
    i) If a defendant can prove he did not know, and in the exercise of reasonable care had no reasonable grounds to believe that the statement was false, he will not be liable.

Section 5 Exemption Approaches

Tuesday, November 29, 2011
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a. 4(2)
   a. 4(2) exempts transactions by an issuer not involving any public offering. In considering whether an offering is "non public," we consider (1) the number of offerees (not just purchasers); (2) the relationship of the offerees to each other and to the issuer; (3) the number of units offered and size of the offering; (4) the manner of the offering. Under **Ralston Purina**, an offering is "non public" if it is made to people who can "fend for themselves," meaning they have both (1) sophistication as an investor [with experience in issuer's particular industry/biz; wealth can be proxy for sophis if (a) lawyer up or (b) bargaining power] and (2) they have (a) been given disclosure or (b) given access to information a registration statement would contain [either by holding an open house; offeree is so wealthy he has bargaining power; or otherwise in a position to be given access to info]. If one offeree can not "fend for himself" then that ruins application of the exemption.
b. Reg D
   a. General solicitation
      i. Rule 502(c) of Reg D prohibits general solicitation. Need a pre-existing relationship whereby issuer is capable of ascertaining financial status and sophistication of potential investor (In re Kenman; Mineral Lands No Action Letter)
   b. Max offering price
      i. Under Rules 504 and 505, there is a maximum aggregate offering price in reliance on Reg. D. You consider all offerings (1) under 504, (2) under 505, and (3) that violate section 5 of the Securities Act.

   c. # purchasers
      i. Under Rule 501(e), purchasers are defined as anyone who is not, inter alia: (1) a relative or a spouse/relative of a purchaser with the same residence; or (2) an accredited investor. An accredited investor is who falls within (or reasonably is believed to fall within) one of the enumerated categories in 501(a) including: (1) various financial institutions; (2) directors, executive officers, general partners of the issuer of the securities being offered (which includes president, VP, etc per 501(f)); (3) corporations with assets exceeding $5M; (4) natural persons when, at time of purchase (a) have a net worth of over $1M or (b) have an income of $200k individually or $300k jointly with spouse and a reasonable expectation of reaching the same income that year.

   d. Disclosure for non-accredited
      i. Under Rule 502(b)(1), if the issuer is selling under 505 or 506 to non-accredited investors, the issuer **must furnish** to such purchaser information set out in Rule 502(b)(2) (which, in turn depends on whether the issuer is a reporting company or not) a reasonable time prior to sale.

   e. Resale restrictions for 505 & 506
      i. Securities acquired in a transaction exempt under Reg D are restricted and cannot be re-sold without registration or an exemption from section 5. As such, issuers must (and do) take precautions to ensure that any resales are limited. Under Rule 504 transactions, there is no meaningful limit on resales so long as the offering complies with applicable state law registration requirements.

   f. Substantial compliance
      i. Under Rule 508, if there is a mistake in your Reg D offering that (1) never affected the complaining party; (2) issuer made an attempt to comply with all standards; AND (3) the mistake was insignificant with respect to the offering, then the mistake doesn't result in loss of the exemption. A mistake is not insignificant, and hence any mistake relating to the following, result in loss of the exemption: (a) maximum offering amount not complied with; (b) number of purchasers; (c) prohibition of general solicitation.

   g. Integrating Reg D Offerings
      i. The integration doctrine examines separate offerings and sales and considers whether they ought to be considered one. First, consider timing. Reg D offerings have a safe harbor under 502(a) of no-integration for 6 months, so if another offering was made outside of those 6 month periods, we presume no integration. If another offering was made outside of the 12 month windows before and after the current offering, that is conclusive proof to not integrate. If the other offering comes within those 6 month periods, apply the integration factors. The integration factors are used to determine whether separate offers and sales should be integrated: (1) single plan of financing; (2) same class of securities; (3) same time period (again, SHs); (4) same type of consideration; (5) money raised for the same general purpose.

c. Intrastate offerings
   a. 3(a)(11)
      i. Under 3(a)(11), securities offered and sold by local companies to local investors to finance local projects will be exempt from section 5 registration. Investor-offerees must be residents of the state, determined by their domicile. A single offer to an out of state resident will ruin use of the exemption. The company must be incorporated and do business in the state (significant income-producing biz in the state). The money raised has to finance local projects. A purchaser of securities offered under this section may re-sell to other in-state residents without restriction. But before a purchaser may re-sell securities to out of state residents, the securities must "come to rest" in state, meaning that the initial resident purchaser purchased with "investment intent."

      ii. Resales
         1) A purchaser of securities offered under 3(a)(11) [and Rule 147] may resell without restriction to another bona fide resident of that state.

2) For an offer or sale by a purchaser to a nonresident to be permitted, however, the issue of the securities offered must have "**come to rest**."
3) Securities must "**come to rest**" in-state in order to re-sell out of state. Securities "come to rest" in state when an in-state resident purchases the security with investment intent.

iii. Integration problem
1) If a company does separate national offerings that are qualitatively similar to the 3(a)(11) offering, and are close by in time, you have to be wary that your 3(a)(11) offering will integrate into other states and ruin the exemption.

b. Rule 147
i. Under Rule 147, the intrastate offering safe harbor, if you satisfy the requirements in the rule, your offering can benefit f rom the 3(a)(11) exemption.

ii. Integration
1) Under Rule 147(b), offerings (504, 505, 4(2), 506, and registered ones) that fall outside the 6mo window of before and after the Rule 147 (and 3(a)(11)) transaction will not be integrated.

iii. Nature of Issuer
1) An issuer can use this exemption so long as (1) the issuer is incorporated in the state; (2) the issuer does business in the state by (a) getting 80% of consolidated gross revenues from operations in the state; (b) 80% of consolidated assets are held in the state; (c) 80% of net proceeds of the offering will be used in the state; and (d) its principal office is in the state.

iv. Offeree residence
1) Offers and sales can only be made to people resident (note: not domiciled) within the state, meaning that the state is the person's principal residence at the time of the offer/sale. All offerees must be residents, any non-resident offeree will ruin application of the exemption.

v. Resales
1) A purchaser of securities in a Rule 147 (and 3(a)(11)) intrastate offering can freely re-sell the securities to other resident investors, but in order to be able to re-sell to out-of-state investors, the securities must "come to rest." Per Rule 147(e), securities "come to rest" 9 months after the offering (date of the last sale). After 9 months have elapsed, residents may freely sell to out of state residents. They are unrestricted securities.

vi. General solicitation is totally OK.

d. Resale Exemptions
a. 4(1)
i. Underwriters
1) Any person who purchases securities from an issuer with a view towards distribution. [Gilligan]
2) A person who offers or sells for an issuer in connection with a distribution
3) Any person who directly or indirectly participates in the offering, selling or underwriting process for an issuer in connection with a distribution. [SEC v. Chinese Consolidated Benevolent Ass'n]
4) Any person who purchases from a control person when such purchase is a part of the control person's distribution.
5) A person who sells for a control person when such assistance is a part of the control person's distribution. [Wolfson]

ii. View towards distribution
1) "view towards" means the person had an intention to resell, not for investment purposes. First we look at the length of time the investor held the security. (1) if investor holds for less than 2 years, presume intent to distribute (and may rebut by showing intent to invest; changed circumstances); (2) **if investor holds for 2** or more years, presume investment intent; (3) if investor holds for 3 or more years, investment intent is conclusive. Then we look at any facts indicating investment intent or changed circumstances.
2) Per Ralston Purina, "distribution" is one that is public. If the distribution is made to (1) people who can "fend for themselves," who are sophisticated and have access to information; OR (2) the offerees/resale investors could have participated in the initial exempted distribution in which the potential U/W purchased from the issuer, then that is not a "distribution" and hence the person is not an U/W.

iii. Participates
1) A person who participates in the issuer's the offering for the issuer's benefit (either by continually soliciting the securities or hyping the securities to help the issuer; consider extent of help and involvement), in connection with the distribution of a security is also deemed an U/W for 4(1) purposes. The participant need not be paid, hired by the issuer, or even known by the issuer to be an U/W in this fashion.

b. Rule 144
i. Rule 144 is a safe harbor for a transaction involving a restricted security resale. If a sale of securities complies with Rul e 144, (1) an affiliate or other person who sells restricted securities will be deemed not to be engaged in a distribution and therefore not an U/W for that txn; (2) person who sells her securities on behalf of an affiliate of the issuer will be deemed not to be engage d in a distribution and therefore not an U/W of the affiliate; and (3) purchaser in such transaction will receive securities that ar e not restricted. Hence, your resale can benefit from 4(1).
1) **General (144(b)(1) and (2))**
a) **Holding Period for Restricted Securities (144(d))**

b) **Current Public Information (144(c))**

2) **<u>Affiliate Only</u> (144(b)(2))**
   a) **Volume Limit (144(e))**
   b) **Manner of Sale Limitation (144(f),(g))**
   c) **Notice Requirement (144(h))**

ii. Per Rule 144(a)(1), an affiliate of an issuer is a person who, directly or indirectly, controls the issuer. Affiliates are of ten (1) officers (2) directors or (3) shareholders of 10% or more of the issuer.

iii. To utilize Rule 144, a person must meet two general requirements. (1) the person seeking to sell the restricted securities mu st meet the holding period established in Rule 144(d). This holding period is 6mo for restricted securities of Reporting issuers and 1yr for restricted securities of non-reporting issuers. This holding period runs from the date of purchase from the issuer or from an affiliate of the issuer, whichever is later. For unrestricted securities, the holding period is zero. (2) there must be ad equate current information concerning the issuer per Rule 144(c). For non-affiliates with reporting issuers, the info requirement runs for 1 yr. For non-affiliates of non-reporting issuers, there is no information requirement. If the issuer is a reporting company, it may comply with this section by complying with the reporting requirements; if the issuer is non-reporting, the issuer can publicly make information available per Exch. Act Rule 15c2-11. Affiliates must always satisfy this requirement. Non affiliates of reporting companies have a one year information period to make sure the company is current on their reporting requirements.

iv. There are three additional requirements for affiliates.

v. Volume Limitation. Rule 144(e)(1) places restrictions on the amount of sales of equity security an affiliate can make during a given period of time in reliance on the rule; the amount of securities sold by the affiliate, plus all the sales of securities of the same class sold in the last 3 mo, can't exceed the greater of: (a) 1% of shares of that outstanding class or (2) the average weekly trading volume for the 4 weeks preceding the filing of notice of proposed sale per Rule 144(h). For purposes of calculating the cap, you consider both registered and unregistered securities, with some exception. The types of securities not counting towa rds the volume limitation are (1) securities sold by the affiliate in a registered offering (affiliate sold shares under a regist ration statement during a PO); (2) securities sold in a transaction exempt under section 4 and private offerings.
   1) Purpose is to ensure a large amount of sales by an affiliate won't disrupt the market by having tons of securities enter mkt at once (which may cause stock price to drop temporarily)

vi. Manner of Sale. Per 144(f), an affiliate must sell the securities in an unsolicited brokers' transaction within the meaning of section 4(4); the affiliate cannot solicit or arrange for the solicitation of orders to buy securities in connection with the se transactions. The affiliate also cannot make any payment in connection with the offer or sale to any person other than the br oker or dealer who executes the order.

vii. Notice Requirement. Per Rule 144(h), Affiliates using Rule 144 must file a Form 144 with the SEC. Form includes information on relationship to issuer, nature of the securities, how they were acquired and the proposed amounts of securities to be sold.

c. Rule 144A
   a) Rule 144A allows resale of restricted securities to qualified institutional buyers (QIBs) by persons other than the issuer of such restricted securities. If Rule 144A conditions are met, then the offer or sale of securities can benefit from 4(1) because t he sale isn't a "distribution" so the person is not an U/W. the purchaser of securities under Rule 144A receives restricted securitie s.

   b) Selling to a QIB?
      1) QIBs are entities that are in the business of investing. They are: (1) enumerated in Rule 144A(a)(1)(i) acting for their own accounts that in the aggregate owns and invests at least $100Min securities, such as (a insurance companies; (b) investment companies; (c) employee benefits plans; (2) dealers; (3) investment companies (eg. Mutual funds); and (4) banks that (a) that in the aggregate own and invest $100M in securities and (b) that have an audited net worth of at least $25M as per its latest annual financial statement. People cannot be QIBs.
      2) The seller must reasonably believe that the purchaser is a QIB.
   c) NO HOLDING PERIOD?
   d) Seller can generally solicit
   e) Seller notify purchaser that relying on Rule 144A and restricted securities being sold?
      1) Rule 144A(d)(2) requires that the seller take reasonable steps to notify the QIB that the seller is relying on Rule 144A as an exemption from registration. This may be achieved by (1) placing a legend on the securities indicating their restricted status and that they can only be sold via a reg. stmt or an exemption; and (2) include statements in the private placement memorandum making this clear.

   f) Securities sold aren't same class of securities that are listed on nat'l securities exchange
      1) Per Rule 144A(d)(3), the transaction for which the exemption applies cannot cover securities of the same class (at time of issuance) as securities listed on a national securities exchange.

   g) Disclosure
      1) Per Rule 144A(d)(4), upon request to the issuer, a non-reporting issuer must provide to the holder and to the prospective QIB-purchaser certain basic information concerning the issuer's business, products and services, and its financial statements. Reporting issuers have no such obligation.

   h) Integration
      1) Per Rule 144A(e), prior and subsequent sales of the same securities as that offered/sold via Rule 144A will not be vertically integrated.

d. Section 4(1½)
   a) Section 4(1½) is an exemption that permits affiliates and non-affiliates to make private sales of securities held by them so long as

(1) the offeree-investors are able to "fend for themselves" within the meaning of Ralston Purina [sophistication and access]. An affiliate or non affiliate using 4(1½) will be deemed not to be an U/W; and for an affiliate, the broker and purchaser won't be deemed U/Ws because there is no distribution. Also, (2) there is no holding period (3)and generally no general solicitation or wide distribution permitted.

e. Control Person Resales
   i. A control person is someone that has control, and control is defined in Rule 405 as the possession, direct or indirect, of th e power to direct or cause the direction of the management and policies of a person, whether through the ownership of voting securiti es, by contract, or otherwise. This means that a control person (1) has the power to control the management and policies of the issuer; or (2) can compel the issuer to obtain signatures necessary to file a registration statement covering the control per son securities. You can also consider (3) percentage of stock ownership, (4) director or officer position held; and (5) relations hip with insiders. This means that directors, executive officers, controlling shhs may be control persons

   ii. Control persons must be careful of being deemed U/Ws or having someone else being deemed an U/W for the control person in that transaction. Even when control ppl acquire unrestricted shares, there is still a chance that someone in the txn is an U/ W.
   iii. Control persons may use 4(1) so long as there is no U/W in the transaction
      1) Control person as U/W. If Control person held for 2 or more years, then there's presumptive evidence of investment intent sufficient to say he's not an U/W. with 3 years, it's conclusive that the security "came to rest." If the control person acquired an unrestricted security, he himself cannot be an U/W for the issuer because that security has already come to rest. If the control person acquires a restricted security, he can be an U/W if "view towards" and "distribute."
      2) Purchase from a control person. A person who purchases securities from a control person can be deemed an U/W if they **purchased in the issuer's distribution** "with view towards distribution."
      3) Assists a control person by soliciting or participating in **distribution**. A person, such as a broker, may be deemed an U/W for the control person if the control person is "distributing"
   iv. Control persons may use 4(1½)
      1) If the control person is conducting a private transaction to ppl who can "fend for themselves," three things happen:
         a) Control person won't be doing a "distribution" so he's not an U/W;
         b) The broker won't be helping in a "distribution" so he's not an U/W;
         c) And the purchaser won't have acquired the securities in a "distribution," so he's not an U/W, unless it later turns out that the purchaser re-sold within a day to 300 retail investors.

10b-5 Approach

Wednesday, November 30, 2011
2:19 PM

1. Jurisdictional nexus
    1. The fraud must have occurred via a means or instrumentality of ISC.

2. Transactional nexus
    1. Plaintiff must have purchased or sold a security.
    2. Defendant can be anyone whose fraudulent activity was made "in connection with" the purchase or sale of a security

3. There must have been a material misstatement or omission
    1. Misstatement or omission?
    2. Materiality
        i. A fact is **material** per **TSC** when a reasonable investor would think the fact would significantly alter the total mix of information
            1) Two ways to measure: measure magnitude via some metric; look at stock price change at disclosure of truth.
            2) When considering the magnitude, one popular rule of thumb is to look at whether the stmt relates to 5% of earnings, revenues, or income. If it relates to more than 5% of earnings, revenue, income, then it's likely material. Then, you have to consider qualitative factors to put the #s into perspective. "that particular misstatement allowed the company to meet expectations/mask a change in earnings. "
            3) When looking at stock price, (1) when was the truth really revealed into the mkt? on one hand, this could be the date.. On the other hand, this could be the date. (2) did the stock price change? Was there some other reason the stock price changed? (a) confounding events from the market or the firm; (b) overall market movement; information leaked; (c) market not efficient; (d) market is irrational.

        ii. Defenses
            1) Truth on the Market Defense. If the misstatement or omission was already part of the "total mix" of information in the market, then the misstatement or omission cannot be material by definition.
            2) Opinions and puffery may not be actionable as facts.

        iii. Forward-looking statements
            1) A statement regarding **forward looking information** is material by balancing both (1) the indicated probability that the event will occur; and (2) the anticipated magnitude of the event in light of the totality of the company activity. The probability is assessed by looking at indicia of interest at the highest levels such as (a) board resolutions; (b) actual negotiations; (c) CEO's involvement, amongst other things. The magnitude is assessed by considering (a) the size of the entities involved and (b) the potential premiums over the market.
                a) A statement concerning forward-looking information is not maerial under the Exchange Act 21E(c)(1) safe harbor, which (1) states that forward-looking statements are not actionable if they are (a) identified as forward-looking and (b) is accompanied by a meaningful cautionary statement OR (3) are not material.
                b) Only reporting issuers may use this safe harbor. It is not valid during IPOs.
                c) A cautionary statement is meaningful when it discloses the risks that pose the greatest possibility of undermining projections when made. When those risks change, it is important to either (1) tailor the cautionary statement or (2) tailor the forward looking statement accordingly.

    3. Scienter
        i. Per **Hochfelder**, the plaintiff must establish that the defendant acted with knowledge, intent, and in some instances, recklessness (a conscious awareness that the representation made has a significant chance of being false, even if no knowledge as to its falsity).
        ii. When the SEC brings an enforcement action, it need not prove the purchaser/seller of securities relied.

    4. Reliance
        i. Under 10b-5, the plaintiff must show that alleged misstatement (1) affected the market price and/or (2) plaintiffs' decision to transact.
            1) Ie. that plaintiff transacted/transacted at that price in reliance on the misstatement/omission.
        ii. If the transaction occurred face-to-face, the plaintiff may prove reliance the old fashioned way.
        iii. Per **Basic**, reliance is presumed when an investor buys or sells a security in reliance on the integrity of the stock price in an efficient market. In order to invoke the presumption, a plaintiff must prove (1) the defendant made a public misrepresentation; (2) that was material (3) the shares were traded on an efficient market; and (4) the plaintiff traded the shares between the time the misrep was made and the time the truth was revealed.
        iv. The defendant can rebut the presumption of reliance with any showing that "severs" the link between the alleged misrep and (1) the market price or (2) plaintiffs' decision to trade. He may do so by arguing (1) the market was not deceived (the truth had entered the mkt; corrective stmts were made; plaintiffs knew); (2) those plaintiffs would have sold for other reasons anyway; and (3) the market for securities is not efficient.
            1) In order to prove a market for securities is not efficient, consider the Cammer factors: (a) the average weekly trading volume; (b) the number of securities analysts following and reporting on the security; (3) presence of market makers dealing with the security; (4) company's eligibility to file Form S-3; (5) cause and effect relationship between unexpected corporate news and changed in price of the security (how fast the market has reacted in the past); (6)

company market cap.

5. Loss Causation
    i. Per **Dura**, plaintiff must prove that defendant's materially misleading representation caused the drop in price that caused plaintiff's damage.

6. Damages
    i. Under 10b-5, plaintiffs are entitled to their out of pocket damages, equaling the K price - the security's true value at the time of the transaction. Defendant will argue the security was valued highly on the day of the transaction because the market knew everything and was able to internalize all info. Plaintiff will argue tha the true value of the security was way lower because there was a lot the market did not know.
    ii. Per Section 28(a) of the Exchange Act, the plaintiff cannot recover any more than his actual damages, meaning he is not entitled to punitive damages.

Gun Jumping Cheat Sheet

Gun Jumping Rules Cheat Sheet

a. **Pre-Filing**
- i) No sales - §5(a); No offers - §5(c)
- ii) **2(a)(3) Offer - any oral/written commct'n conditioning public mind**
  - i. **Motivation of comm**
  - ii. **Type of info (hard/soft)**
  - iii. **Breadth of distribution**
  - iv. **Form of comm (written, reproduce)**
  - v. **Particulars of offering mentioned**
- iii) **SH/ "offer"**
  - Rule 135 – **short, factual notices** announcing a proposed registered offering
  - Rule 163 – communications prior to the filing of the registration statement by **WKSIs**
  - Rule 163A – statements prior to **30 day period before** the filing of the registration statement
  - Rule 168 – regularly released factual and forward-looking information by **reporting** issuers
  - Rule 169 – regularly released factual information by **non-reporting** issuers

b. **Waiting Period**
- i) No sales - §5(a); 5(b)(1) - transmit prospectus complies w/ §10
- ii) **2(a)(10) Prosp - any written/broadcast commct'n offering a security**
- iii) **Is it written or broadcast?**
- iv) **SH/"offer"**
- v) **SH/ "prospectus"**
  - 2(a)(10)(b) - Oldschool tombstone ad
  - Rule 134 - Extensive tombstone ad
  - Roadshows/oral communications
- vi) **Comply with section 10**
  - 10(a) - Final statutory prospectus
  - Rule 430 - Preliminary prospectus
  - Rule 164 / 433 - FWP

c. **Post-Effective Period**
- i) Can sell; Can offer; 5(b)(1) - prospectus must comply w/ §10; 5(b)(2) - Can't deliver a security unless preceded/accompanied by a final §10(a) prospectus
- ii) **5(b)(1) 2(a)(10) prosp any written/broadcast commctn offering security**
  - i. **Same as above**
  - ii. **SH/Prospectus - 2(a)(10)(a) - traditional free writing**
  - iii. **Can't use Rule 430 prosp for anything**
- iii) **5(b)(2) Delivery applies to everyone except:**
  - 174(b) **Reporting issuers - no delivery req.**
  - 4(1) anyone not an issuer, U/W, dealer - **secondary market**
  - 4(4) **unsolicited broker's transactions**
  - 4(3) & 174(b) **dealers and U/Ws who sold their allotment**, but not:
    - **174(d)** within **25d period for non-reporting issuer but listed on exchange**
    - **4(3)(A)** within **40d period** for **seasoned offering** [not listed on exch, not IPO either]
    - **4(3)(B)** within **90d period for IPO**
    - **4(3)(C) & 174(f) U/Ws selling their allotment** [forever delivery req.]
    - 174(h) obligation to deliver under section 4 or Rule 174 can be satisfied by Rule 172 access=delivery
- iv) **If delivery req., sufficient under 5(b)(2)?**
  - Rule 172 access=delivery if **reg stmt filed** and **10(a) prosp filed**
- v) **If delivery req, must notify**
  - Rule 173 - must provide with 10(a) prosp or notice that they would have been entitled to one w/in **2 days of completion of sale**.

Pre-filing
- Forward looking stmts OK: Rule 163 (pre-filing; WSKI only); Rule 168 (pre-filing, reporting Only)
- Can refer to the offering: Rule 135; Rule 163 (WKSI only)
- U/Ws cannot use any SH in the pre-filing period.

Legend needed
- Rule 135
- Rule 163 WKSIs (if written commctn)
- Rule 430? A red herring legend
- Rules 164/433 - FWP - required
- Rule 134 - unless oldschool tombstone; unless accompanied/preceded by section 10 prospectus.
- Rule 147

Waiting period & post-effective
- Can refer to the offering: Rule 134; 2(a)(10)(b); Rule 164/433 FWP
- Fwd-looking/detailed financials: 10(a) and Rule 430 prosps; Rule 164/433 only (not Rule 134)
- U/Ws can use: Rule 134 (waiting period only- first time U/Ws can reference the offering); can use Rule 433 for FWPs

Civil Liability Cheat Sheet

Section 11

Plaintiffs - must be able to **trace**; must have **purchased**
Defendants - 11(a)(1) issuer, directors, signatories per 6(a);
- 11(a)(2) directors at time; 11(a)(3) ppl named as or about to be directors on reg stmt; 11(a)(4) experts for their portion; 11(a)(5) U/Ws; control persons (15)

11(a) Prove - Material misstmt/omission
- Materiality
  - Historical: **TSC**; 5% of earnings, revenue, income; stock price
  - Fwd-looking: **TGS** probability x magnitude of anticipated event
    - Prob = indicia of interest at highest levels
    - Magnitude = size of entities and pot'l premium
- Defenses
  - Truth on market
  - Opinions/puffery
  - **27A(c)** Fwd-looking SH (reporting only; no IPO)
    - **27A(i)(1)** "Fwd looking stmt"
    - **27A(c)(1)(B)** P prove knowledge?
    - **27A(c)(1)(A)** Meaningful cautionary stmt?

Defenses
- **11(e)** No loss causation
- **11(b)(3)** Due diligence
  - **11(b)(3)(A)** non expert/non expertised
  - **11(b)(3)(B)** non expert/expertised
  - **11(b)(3)(C)** expert/expertised
  - What did they know, given position?
  - **Rule 176** - investigation, affirmative action, written record, corp minutes, material Ks.
- **11(a)** P already knew
- **11(a)** Reliance (1yr earnings)
- **11(b)(1)** Whistleblower
- **13** SOL

11(e) Damages - **K price minus**
- **Resale price if P resells before suit**
- **Value @ t file suit if P holds until jmt final**
- **Resale (if more than value @ t suit) if resell after file suit**

11(f)(1) Joint & several

Section 12(a)(2)

Plaintiffs - must have purchased; prosp delivery requirement
- **174(b)** No delivery for reporting issuers
- **4(1)** no delivery for secondary mkt sellers
- **4(4)** no delivery for unsolicited brokers' transactions
- **4(3)** no delivery for dealers/ U/Ws who sold allotment EXCEPT
  - **174(d) 25d non reporting but listed on nat'l exchange**
  - **4(3)(B) 40d for seasoned offering**
  - **4(3) 90d for true IPO**
  - **4(3)(C) & 174(f) U/Ws selling allotment FOREVER req.**

Defendants - "sellers"; solicitors; **159A** issuer in firm underwriting when purch in initial distr.; control persons (15)
Prospectus is 10(a), FWP, relating to PO
Material misstmt/omission
- Historical: **TSC**; 5% of earnings, revenue, income; stock price
- Fwd-looking: **TGS** probability x magnitude of anticipated event
  - Prob = indicia of interest at highest levels
  - Magnitude = size of entities and pot'l premium
- Defenses
  - Truth on market
  - Opinions/puffery
  - **27A(c)** Fwd-looking SH (reporting only; no IPO)
    - **27A(i)(1)** "Fwd looking stmt"
    - **27A(c)(1)(B)** P prove knowledge?
    - **27A(c)(1)(A)** Meaningful cautionary stmt?

12(a)(2) Reliance - focus on mkt as a whole, P need not have received
Defenses
- **12(b)** No loss causation
- **12(a)(2)** Reasonable care
- **13** SOL
- **12(a)(2)** P already knew

Damages

Section 12(a)(1)

Plaintiffs - must have purchased from "seller"
Defendants - "sellers", solicitors (**Pinter**); control persons (15)
Prove - D violated section 5 in transaction to plaintiff
Defenses
- 13 SOL - 1 yr from disco
- Exemption applied

Damages
- Rescission if not already resold
- Rescissionary damages purch - resale price

10b-5

Jx nexus
Txn nexus - P must have purchased/sold
Material misstmt/omission
- Historical: **TSC**; 5% of earnings, revenue, income; stock price
- Fwd-looking: **TGS** probability x magnitude of anticipated event
  - Prob = indicia of interest at highest levels
  - Magnitude = size of entities and pot'l premium
- Defenses
  - Truth on market
  - Opinions/puffery
  - **27A(c)** Fwd-looking SH (reporting only; no IPO)
    - **27A(i)(1)** "Fwd looking stmt"
    - **27A(c)(1)(B)** P prove knowledge?
    - **27A(c)(1)(A)** Meaningful cautionary stmt?

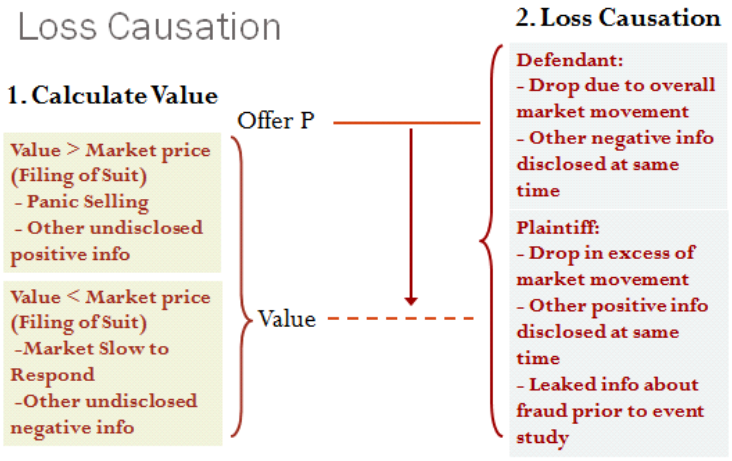
Scienter - **intent, knowledge, recklessness**
Reliance
- **Fraud on mkt theory**: P prove: D made public misstmt; was material; P purchased after misstmt before disclo; mkt efficient
- **D rebut**: Mkt not deceived (truth disclo already); P would have sold anyway; mkt in securities not efficient
  - **Cammer factors: av weekly trading vol; presence of analysts closely following and reporting; presence of mkt makers; cause and effect relationship in the past**
- Then prove reliance old-fashioned way

21D(b)(4) Loss causation
Damages - out of pkt calculation

Loss Causation

i) D argument
   a) D is only liable for the damages the misstatement caused, and not all of the loss is attributable to the misstmt; there were external factors.
      1) Confounding events
         1) From firm: other negative events disclosed on that day
         2) From market: something bad happened in the industry
      2) Other undisclosed positive info
         1) The drop is excessive, there was other positive info that the mkt didn't know, and had they known, drop wouldn't have been as drastic
      3) Irrational behavior in reaction to news
         1) Panic selling; mkt didn't understand; only got partial information
      4) Drop due to overall market movement
         1) Create a basket of stock and track how that basket did relative to this company
         2) Behaved like other similar companies that did a PO during the same itme

ii) Plaintiff argument
   a) Logical link between disclosure date and the drop in price
      1) The other negative info was NOT significant; was already released into mkt so it wasn't new info
         1) There was other positive info released that day
         2) There was other undisclosed negative info the mkt didn't know so the value here is artificially higher
      2) The market already knew about the fraud prior to this particular date
      3) Market was doing well that day
         1) The drop here was in excess of market movement
         2) The companies you compare to are very different



Issuer Exemptions Cheat Sheet

4(2)

Offering is nonpublic where, under **Ralston Purina**, it is made to people who can "fend for themselves."
A person can fend for himself when he has sophistication as an investor and access to information the reg. stmt. would otherw ise contain.
We also consider a # of factors: # of offerees; relationship of offerees to issuer and to each other; size of the offering; m anner of the offering

Sophistication as an investor
Access to info: Bargaining power; Relationship w/ issuer

Reg D

501(a) defines **accredited investors**.
502(c) prohibits general solicitation in the offer/sale of securities - there is no general solicitation when the offeror has a pre-existing relationship such that they can evaluate/assess the offerees financial circumstances and sophistication.
Pre-existing relationship is just a proxy for ability to assess financial circ. and sophistication

504 of Reg D exempts a **non-reporting** issuer from offering securities for up to $1M in the aggregate, counting 504, 505, and offerings tha violate section 5, to an unlimited amount of accredited investors and unaccredited investors. **504(b)(2).** General solicitation is permitted according to state law.

504(a)(1)	Only NON REPORTING ISSUERS
504(b)(2)	$1M
504(b)(2)	No limit on # purchasers
	Gen solicit OK

505 of Reg D exempts offerings for up to **$5M** in the aggregate to unlimited accredited and up to 35 unaccredited investors. **505(b)(2).** General solicitation is prohibited under 502(c). Also, the issuer must afford the **non-accredited investors with certain information a reasonable time before sale under 502(b)(2).** Also, the issuer must take reasonable care to notify of the restricted nature of the securities under **502(d)** by placing a **legend** in the certificate, etc.

505(b)(2)	$5M
505(b)(2)	35 non accredited
502(c)	General solicitation prohibited
502(b)(1)	Provide non-accredited w/ certain info set out in **502(b)(2)** & advise of resale limits reasonable time before sale
502(d)	Take reas care to notify all purchasers of restricted nature of securities; legend; written disclo

506 of Reg. D exempts offerings for an unlimited offering price to an unlimited amount of accredited investors and up to 35 non-accredited but sophisticated investors capable of evaluating the merits and risks of the investment. **506(b)(2)**. General solicitation is prohibited under **502(c)**. Also, the issuer must afford the **non-accredited investors with certain information a reasonable time before sale under 502(b)(2)** . Also, the issuer must take reasonable care to notify of the restricted nature of the securities under **502(d)** by placing a **legend** in the certificate, etc.

	Unlimited offering price
506(b)(2)	35 non accredited but sophisticated, capable of evaluating merits and risks
502(c)	General solicitation prohibited
502(b)(1)	Provide non-accredited w/ certain info set out in **502(b)(2)** & advise of resale limits reasonable time before sale
502(d)	Take reas care to notify all purchasers of restricted nature of securities; legend; written disclo

Under 508 of Reg D, an immaterial failure to comply w/ a requirement of Reg. D won't ruin the exemption if the mistake:
Never affected the complaining party;
the issuer made an attempt to comply; and
the mistake is insignificant wrt the offering as a whole. Significant mistakes are # purchasers; aggregate price, and general solicitation.

3(a)(11) exempts intrastate offers by local companies to local residents to fund local projects. All offerees and purchasers must be l ocal residents, as defined by their **domicile (reside w/ intent to remain)**. Next, the company must be incorporated in the state and must conduct significant income-producing activities in the state. Lastly, the money raised from the offering must go towards a project in the state. The fact that the issuer purchased raw mat erials outside of the state in order to do the project in-state satisfies this standard.

Rule 147 exempts intrastate offers by local companies to local residents to fund local projects. All offers and sales must be made to local residents as defined by their **principal residence at the time of the offer**. **147(d)(2).** The company must be incorporated in the state **(147(c)(1))** and must derive 80% of gross revenues from the state and must have 80% of their total assets in the state. **147(c)(2).** The company must also have its principal office located in the state. **147(c)(2).** 80% of the money raised in the offering must go towards a project in the state. **147(c)(2)**. Under **147(f),** the issuer must place a **legend** on all securities to inform purchasers of their restricted nature.

147(d)(2)	Local residents, determined by principal residence at time of offering
147(c)(1)	Co must be incorp. In state
147(c)(2)	80% gross revenues derived from state; 80% assets held in state
147(c)(2)	Principal office located in state
147(c)(2)	80% money raised must fund local project
147(f)	Must place legend on all securities to inform purchasers of restricted nature

INTEGRATION

The integration doctrine considers whether seemingly separate offerings ought to be considered one.
There are several factors to apply:

Single plan of financing
Money raised to fund same project
Same class of securities
Same consideration given
Existence of SH

SHs

Reg D's 502(a) provides that offerings outside of the 6mo period before and after the Reg D offering will not be integrated. If the other offering falls within that 6mo period, then the factors will be applied.

Rule 147(b) provides that offerings made outside the 6mo period before and after the Rule 147 offering will not be integrated ; if they fall w/in that 6mo period, then the factors apply.

3(a)(11) does not have a SH
4(2) offerings do not have a SH

Resale Exemptions Cheat Sheet

4(1) permits a resale transaction when there is no U/W as defined in 2(a)(11). An U/W, inter alia, is a person who purchases from an issuer with a view towards distribution.

One way to refute U/W status is to prove "investment intent."

For investment intent we look at:

time held and any presumptions coming from it

anything indicating investment intent

changed circumstances.

SEC does not favor this changed circumstances approach.

Another way to refute U/W status is to prove there was no distribution under **4(1 1/2).**

Fend for self

Under **Ralston purina**, there is no distribution if the sale is made to people who can "fend for themselves," considering both sophistication and a ccess to information.

Conduit approach

Under the conduit approach, if the resale purchaser could not have participated in the original offering in which the potenti al U/W purchased, then it looks more like a "distribution."

Rule 144 exempts resales so long as all the requirements are met. First, is ____ an affiliate? An affiliate under **144(a)(1)** is typically a 10% or more shh, an officer, or a director of the issuer. Is ____ a shh/officer/director?

Affiliate

Holding period 144(d)	6mo (reporting) 1yr (non reporting) 0 (unrestricted secs)
Current public info 144(c)	ALWAYS
Volume limit 144(e)	Securities sold now + same class in 3 mo can't exceed greater of: 1% of outstanding class of shares; av weekly trading volume in past 4 wks Securities sold under a reg stmt and sold under a 4(1) or 4(1 1/2) txn don't count
Manner of sale 144(f), (g)	Unsolicited broker's transaction Can't solicit or arrange for solicitation; cant pay more than customary fee
Notice 144(h)	Must file Form 144

Non Affiliate

Holding period 144(d)	6mo (reporting) 1yr (non reporting) 0 (unrestricted secs)
Current Public Info 144(c)	1 yr (reporting) 0 (non reporting)

Rule 144A exempts resales to QIBs (144A(a)(1)) for classes of securities that are not listed on a nat'l exchange (144A(d)(3)) so long a s the seller takes reasonable steps to notify the QIB of the resale limitations (144A(d)(2)). Also, for non -reporting issuers, upon request from the purchaser, the seller must provide certain reasonably current basic information about the issuer. 144A(d)(4).

144A(a)(1)	QIB
144A(d)(3)	Classes of securities NOT listed on nat'l exchange
144A(d)(2)	Reasonable steps to notify QIB of resale limts; legend
144A(d)(4)	NON REPORTING ISSUERS, upon request from purchaser, must provide certain reasonably current basic info about the issuer
144A(e)	General solicitation to QIB is OK and won't ruin previous exemptions

Status of securities under issuer exemptions

4(2)	Securities obtained in a **4(2)** offering are restricted and can only be freely resold when they come to rest, either by: (1) registering them; (2) holding them for 3 or more years conclusively; (3) selling them under Rule 144 txn.
Reg D	Securities obtained under a **Reg D** offering are **restricted** and only if they (1) are registered (2) come to rest by being held for 3 or more years (conclusively); (3) are re-sold under Rule 144 and hence "cleansed."
3(a)(11)	Securities obtained under a **3(a)(11)** offering are restricted and can only be freely re-sold to other state residents, but can be freely re-sold to outside residents when the securities "come to rest," meaning they were purchased with "investment intent."
Rule 147	Securities obtained under **Rule 147** are restricted and can be freely resold to other state residents, and can be freely re-sold outside of the state per 147(e) after 9mo after the offering/sale has elapsed.
4(1) and 4(1 1/2)	Securities obtained under 4(1) and 4(1 1/2) if already restricted will REMAIN **Restricted** unless register; hold for 3 or more yrs; resell under 144
Rule 144	Securities obtained under 144 will be CLEANSED and can be freely re-sold
Rule 144A	Securities obtained under 144A are restricted

Is it a Security Cheat Sheet

- Is the instrument a security? This question really is the question of whether the instrument should be regulated by the securities laws
- Is it found in the statutory list **2(a)(1)**?
    - Instruments known as securities
        - **Stocks**
            - Is it labeled stock? [consider investor expectations re. protection of sec laws; would have actually invested in real stock otherwise]
            - Characteristics of stock:
                - **Voting rights in proportion to shares owned**
                - **Right to dividends contingent on profits**
                - **Transferability [can sell to make money, can be pledged as collateral]**
                - **Possibility to appreciate in value**
            - If it has those 4 characteristics, it's stock. Landreth.
            - If not, go on to see if it's an investment K or some other type of security.
        - **Notes**
            - Notes are only securities if they're issued for investment purposes. Commonly, notes have (1) fixed and periodic interested rate; (2) principal amount given by lender and then returned by debtor at maturity date; (3) maturity date for when principal amt returned
            - Is it called a note?
            - Per Reves, presume note is a security
            - Unless bears resemblance to commercial and consumer financing non-security notes:
                - Notes delivered in consumer financing
                - Notes secured by a mortgage on a home
                - Short term notes secured by a lien on small business
                - Notes evidencing character loan from bank to consumer
                - Short term notes secured by assignment of account receivables
                - Notes formalizing open-account debt incurred in ordinary course of business
            - If doesn't bear resemblance, consider 4 factors:
                - **Motivation of buyer/seller to transact**
                    - Security: "seller's purpose is to raise money for general use of a biz enterprise or to finance substantial investments; buyer is interested primarily in the profit the note is expected to generate"
                    - Non security: "note is exchanged merely to promote some commercial or consumer purpose."
                - **Plan of distribution**
                    - Security: "the note was offered and sold to a broad segment of the public which led to common trading for speculation/investment."
                - **Reasonable expectations of investing public that securities laws apply**
                    - Security: "the notes are advertized as "investments" and a reasonable person had no reason to doubt this characterization, securities laws should protect that txn."
                - **Risk reducing factors**
                    - Security: "there are no alternative regulatory schemes that would protect investors in this transaction, such as the existence of collateral, insurance."
                    - Non security: "the notes are insured and collateralized, hence no need to regulate via securities laws."
    - **Specific instruments listed in 2(a)(1)** (fractional oil interest, voting-trust certificate, CD of a security, treasury stock…)
- **Investment Contracts**
    - **Person invests money**
        - Money? Something of value otherwise have gone to capital markets?
        - Investment must be **voluntary** (intent to invest; link to capital markets)
    - **In common enterprise**
        - Horizontal
            - **Pooling of investor assets**
            - **All investors share in same risks/profits of enterprise**
            - Policy: collective action problem, common info desired
        - Vertical Broad
            - **Investor returns/success loosely depend on effort/expertise of promoter**
        - Vertical Narrow
            - **Investor returns/success loosely depend on effort/expertise of promoter & promoter has own stake in outcome**
            - Watch out when promoter gets paid fixed fee
    - **Led to expect profits**
        - Invest to try to get more money; **not just consumption of interest acquired**
        - Types of profits: capital appreciation (value goes up); distributions of earnings (eg. Dividends); fixed returns
        - "investor seems to be motivated by a desire to obtain/consume ___, rather than seeking a return on the acquisition"
    - **Solely from the efforts of others**
        - Need not be 100% efforts of others; sliding scale
        - Consider: **investor involvement undermines policy rationales** [involved in biz, less info asymmetry]; c/a **involvement insignificant, still no access to info;** c/c/a **investor is sophisticated, has bargaining power, whether involved or not, sec laws need not apply**
        - Watch out for investors eligible for referral fees
        - Watch out for enterprise profits contingent on pure luck.
            - Consider: type of info investor would need and whether promoter is the lowest cost provider of that info. If yes, then likely a

security
- Partnerships
  - General partnership interests NOT securities b/c not solely from efforts of others
    - But IS a security if general partner-investor has little ability to control/manage the profits of enterprise:
      - **Agreement leaves little power in hands of investor-partner** [or power is illusory in effect]
      - **Investor-partner lacks experience and knowledge in biz affairs of that enterprise as to be incapable of intelligently exercising his or her pship powers**
      - **Investor-partner is so dependent on a unique entrepreneurial/managerial ability of manager that he can't replace the manager or otherwise exercise meaningful partnership powers** [material Ks made w/ promoter]
  - Limited partnership interests ARE securities bc limited partner is passive and relies on gen partners to manage enterprise.
    - IS NOT security if limited partner has explicit voting power for important matters; veto power; retains control over investment in some other way.
  - Limited liability partnership interests ARE securities because limited partners are not vicariously liable for LLP's debts/obligations, so they are extra passive bc even less incentive to retain control over biz.

- **Are there alternative federal regimes that preclude securities regulation?**
  - FDIC insures it; ERISA regulates the pension plan.

Gun Jumping Cheat Sheet

Gun Jumping Rules Cheat Sheet

a. **Pre-Filing**
- i) No sales - §5(a); No offers - §5(c)
- ii) **2(a)(3) Offer - any oral/written commct'n conditioning public mind**
  - i. **Motivation of comm**
  - ii. **Type of info (hard/soft)**
  - iii. **Breadth of distribution**
  - iv. **Form of comm (written, reproduce)**
  - v. **Particulars of offering mentioned**
- iii) **SH/ "offer"**
  - Rule 135 – **short, factual notices** announcing a proposed registered offering
  - Rule 163 – communications prior to the filing of the registration statement by **WKSIs**
  - Rule 163A – statements prior to **30 day period before** the filing of the registration statement
  - Rule 168 – regularly released factual and forward-looking information by **reporting** issuers
  - Rule 169 – regularly released factual information by **non-reporting** issuers

b. **Waiting Period**
- i) No sales - §5(a); 5(b)(1) - transmit prospectus complies w/ §10
- ii) **2(a)(10) Prosp - any written/broadcast commct'n offering a security**
- iii) **Is it written or broadcast?**
- iv) **SH/"offer"**
- v) **SH/ "prospectus"**
  - 2(a)(10)(b) - Oldschool tombstone ad
  - Rule 134 - Extensive tombstone ad
  - Roadshows/oral communications
- vi) **Comply with section 10**
  - 10(a) - Final statutory prospectus
  - Rule 430 - Preliminary prospectus
  - Rule 164 / 433 - FWP

c. **Post-Effective Period**
- i) Can sell; Can offer; 5(b)(1) - prospectus must comply w/ §10; 5(b)(2) - Can't deliver a security unless preceded/accompanied by a final §10(a) prospectus
- ii) **5(b)(1) 2(a)(10) prosp any written/broadcast commctn offering security**
  - i. **Same as above**
  - ii. **SH/Prospectus - 2(a)(10)(a) - traditional free writing**
  - iii. **Can't use Rule 430 prosp for anything**
- iii) **5(b)(2) Delivery applies to everyone except:**
  - 174(b) **Reporting issuers - no delivery req.**
  - 4(1) anyone not an issuer, U/W, dealer - **secondary market**
  - 4(4) **unsolicited broker's transactions**
  - 4(3) & 174(b) **dealers and U/Ws who sold their allotment**, but not:
    - **174(d)** within **25d period for non-reporting issuer but listed on exchange**
    - **4(3)(A)** within **40d period** for **seasoned offering** [not listed on exch, not IPO either]
    - **4(3)(B)** within **90d period for IPO**
    - **4(3)(C) & 174(f) U/Ws selling their allotment** [forever delivery req.]
    - 174(h) obligation to deliver under section 4 or Rule 174 can be satisfied by Rule 172 access=delivery
- iv) **If delivery req., sufficient under 5(b)(2)?**
  - Rule 172 access=delivery if **reg stmt filed** and **10(a) prosp filed**
- v) **If delivery req, must notify**
  - Rule 173 - must provide with 10(a) prosp or notice that they would have been entitled to one w/in **2 days of completion of sale**.

Pre-filing
- Forward looking stmts OK: Rule 163 (pre-filing; WSKI only); Rule 168 (pre-filing, reporting Only)
- Can refer to the offering: Rule 135; Rule 163 (WKSI only)
- U/Ws cannot use any SH in the pre-filing period.

Legend needed
- Rule 135
- Rule 163 WKSIs (if written commctn)
- Rule 430? A red herring legend
- Rules 164/433 - FWP - required
- Rule 134 - unless oldschool tombstone; unless accompanied/preceded by section 10 prospectus.

Waiting period & post-effective
- Can refer to the offering: Rule 134; 2(a)(10)(b); Rule 164/433 FWP
- Fwd-looking/detailed financials: 10(a) and Rule 430 prosps; Rule 164/433 only (not Rule 134)
- U/Ws can use: Rule 134 (waiting period only- first time U/Ws can reference the offering); can use Rule 433 for FWPs

Rule 135

- **135(a)(1) Legend**
- **135(a)(2)** limited to info:

- **135(a)(2)(i)-(vi),** (i) the name of the issuer; (ii) title, amount, and basic terms of the securities; (iii) the amount of the offering; (iv) the anticipated timing of the offering; (v) a 'brief statement' of the manner and purpose of the offering, without naming the U/Ws; (vi) whether the issuer is directing its offering only to a particular class of purchasers
- **135(a)** no U/W
- All issuers can use

Rule 163

- **163(a)** WKSI (def. 405)
- **163(a)(1)** commct'n considered FWP and prospectus
- **163(b)(1)** legend [issuer will file reg stmt, look at prospectus on website]
  - 163(b)(1)(ii) immaterial/unintentional failure to add legend OK if good faith/reasonable effort comply and FWP amended to include when practicable
- **163(b)(2)** must file commct'n upon filing of reg stmt (unless already filed one, or wouldn't be required to file under Rule 433)
  - 163(b)(2)(iii) immaterial/unintentional failure to file OK if good faith/reasonable effort to comply and FWP filed when practicable
- **163(c)** no U/Ws

Rule 163A

- **163A(a)** commct'n made more than 30d before filing reg. stmt.
- **163A(a)** Does not reference offering
- **163A(a)** Issuer take reasonable steps to prevent further distrib/publication of commct'n during 30d period before reg. stmt. Filed
- **163A(c)** no U/Ws
- All issuers can use

Rule 168

- **168(a)(1)** reporting issuer
- **168(b)(1)** factual biz info [info re issuer, business, financial devel, 'or other aspects of its biz,' advertisements re products
- **168(b)(2)** forward looking info [(i)-(iv)projections re revenues, income, earnings, capital expenditures, dividends, management plans, objectives, future econ performance, assumptions underlying the above]
- **168(d)(1)** issuer prev released/disseminated info in ord course of biz
- **168(d)(2)** consistent in timing, manner, form as past releases
- **168(c)** Cannot reference offering [unless prev releases did]
- **168(d)(3)** U/W can't use

Rule 169

- **169(a)** non-reporting issuer
- **169(b)(1)** factual biz info [info re issuer, business, financial devel, 'or other aspects of its biz,' advertisements re products
- **169(d)(1)** issuer prev released/disseminated info in ord course of biz
- **169(d)(2)** consistent in timing, manner, form as past releases
- **169(d)(3)** commct'n not released to investors or ppl in capacity as investors
- **169(c)** can't reference offering
- **169(b)(2)** no U/W

Rule 134

1. **Reg. stmt. filed**
2. **134(a)(1)-(22)** can only contain what's listed
   a. No fwd-looking projections
3. **134(b)(1) Legend required on all** of these **except**:
   a. **134(c)(1)** Oldschool tombstone Ads. Commct'n that just states from whom can obtain prospectus, the URL, the sec., the price, how order
   b. **134(c)(2)** Communications already preceded/accompanied by a prospectus (430 ok)
   c. A legend may be included, but not required.
4. **134(d) Solicitation of interest**
   a. 134(d) communication preceded/accompanied by section 10 prospectus may solicit offers or ask for recipient's interest if disclaimer ['no offers accepted until reg stmt effective']
5. **134(f)** ok to hyperlink to a prospectus

Rule 433

1) **Reg. stmt. filed**
2) **433(b)(1)-(2)Eligibility**
    a. Reporting/seasoned/WKSI - file reg stmt
    b. Non-reporting/non seasoned - file reg stmt, must accompany w/section 10 prospectus
    c. **433(b)(2)(i)** ok to hyperlink to prospectus
3) **433(c) Information**
    a. Any info so long as doesn't contradict or quality/supersede/modify info in reg. stmt or periodic filings
4) **433(c) LEGEND**
5) **433(d) Filing by date of first use of the FWP**
    a. **Issuer**
        i. 433(d)(1)(i)(A) Issuer free writing
        ii. 433(d)(1)(i)(B) Issuer info used by participants
            1) But not info "derived" from issuer info
    b. **Participant**
        i. 433(d)(1)(ii) If intended to achieve broad unrestricted dissemination
    c. 433(d)(3)-(4) no one needs to file if already filed the FWP; if there's already something filed that has the issuer info in it
    d. **Media**
        i. 433(f)(1) if issuer/participant provides info unaffiliated media, need not comply with (c)(3) and (d) of the rule but the issuer/participant must file the article and include the legend within 4 days of discovering it (unless it's already been filed). If the issuer/participant PAID for the article, then normal rules apply.
6) **Retention**
    a. 433(g) retain non-filed FWPs for 3 yrs
7) **Rule 164(b), (c), (d) Immaterial mistakes** regarding filing, legend, retention are ok if good faith, reasonable care, cured.

Civil Liability Cheat Sheet

Fraud in Prospectus [10(a) & 10(b) FWPs]: 12(a)(2) and 10b-5
Fraud in Reg. Stmt.: 11 and 10b-5
Violation of Section 5: 12(a)(1)
Fraud in Exch. Act Reports: 10b-5
Officer/Director Misstmts/Omissions to Media: 10b-5
Resale Investor Misstmts/Omissions: 10b-5
Insider Trading: 10b-5

Section 11
- ISC
- Plaintiffs - must be able to trace; must have purchased
- Defendants - 11(a) issuer, directors, signatories 6(a); control persons (15)
- Prove - Material misstmt/omission
  - Materiality
  - Defenses
    - Truth on market
    - Opinions/puffery
    - Fwd-looking SH (reporting only)
- Defenses
  - P already knew
  - Due diligence
  - No loss causation
  - Reliance (1yr earnings)
  - Whistleblower
  - SOL
- Damages
- Joint & several

Section 12(a)(1)
- ISC
- Plaintiffs - must have purchased
- Defendants - "sellers", solicitors
- Prove - D violated section 5 somewhere
- Defenses
  - SOL
  - Exemption applied
- Damages

Section 12(a)(2)
- ISC
- Plaintiffs - prospectus delivery req; must have purchased
- Defendants - "sellers"; solicitors; 159A issuer in firm underwriting when purch in initial distr.; control persons (15)
- Prospectus is 10(a), FWP, relating to PO
- Material misstmt/omission
  - Materiality
  - Defenses
    - Truth on market
    - Opinions/puffery
    - Fwd-looking stmt SH (reporting only)
- Reliance - very very loose
- Defenses
  - SOL
  - P already knew
  - No loss causation
  - Reasonable care
- Damages

10b-5
- Jx nexus
- Txn nexus - P must have purchased/sold
- Material misstmt/omission
  - Materiality
  - Defense
    - Truth on market
    - Opinions/puffery
    - Fwd-looking stmt SH (reporting only)

Scienter - intent, knowledge, recklessness
Reliance - fraud on mkt
Loss causation & damages

Section 11 - Fraud in Reg. Stmt.

1. **11(a)** Plaintiff must show tracing for standing
   i) Prove by purchasing from issuer in PO or tracing the securities to the false reg. stmt.
   ii) If IPO, are there outstanding securities of same class/type in the market due to prev. insider/VC Rule 144 offerings? If the insiders/VCs registered their shares as part of the IPO; subject to a lock-up agreement whereby they can't sell until certain time after IPO, plaintiff can easily prove the "pool" is pure IPO secs.
   iii) Difficult to prove tracing in large WKSI markets, P arg. securities laws are designed to protect investors in that very instance, info asymmetry, collective action problem
   iv) No statistical arguments can be made (Krim)
2. **11(a)** Plaintiff must have acquired/purchased a security
3. **11(a)(1)-(5)** Defendants enumerated in statute
   i) **11(a)(1)** every person who signed the registration statement
      i. **6(a) –**includes issuer, CEO, CFO, comptroller or principal accounting officer, and the majority of its board
   ii) **11(a)(2)** directors at time of filing
   iii) **11(a)(3)** people named in reg. stmt as directors/about to become directors
   iv) **11(a)(4)** Experts (accountants, engineer, appraiser (for their part only))
   v) **11(a)(5)** underwriters
   vi) **Section 15** - control persons of any of the above
      i. 405 - person possessing the power to cause/direct management and policies of a person
      ii. 15(a) jointly and severally liable
4. **11(a)** Plaintiff must prove
   i) Untrue statement of material fact;
   ii) Omitted to state a material fact required to be stated therein; or
   iii) Omitted to state a material fact necessary to make the statements therein not misleading
   iv) **Materiality**
      i. When reas. investor would think fact would signif. alter the 'total mix' of info, measured as of time the reg. stmt. becomes effective
      ii. Measure magnitude via % of earnings, revenue, profits; look at stock price as indicator (argue external factors).
      iii. Truth on the market defense [eg. Truth leaked; or another purchaser of same secs. files suit - fraud is public]
5. **11(a)** Plaintiff did to know about the falsity
6. No scienter req. (issuer SL); No reliance req. ; No loss causation req. ; Section 13 SOL, bring w/in 1 yr disco fraud; no more than 3 yrs from offering

7. **Defense's Arguments**
   i) **P already knew**
      i. 11(a) P must not have known
      ii. Also not material ; truth on the market
   ii) **11(b)(3) Due diligence defense** (everyone except issuer can use)
      i. **11(b)(3)(A)** Non experts/non expertised portion - reasonable investigation, reasonable ground to believe and did believe all statements in reg. stmt. true
      ii. **11(b)(3)(C)** Experts/expertised portion - reasonable investigation, reasonable ground to believe and did believe statements in their portion of the reg. stmt. true
         1) 11(a)(4) Experts liable only for those parts prepared by them
      iii. **11(b)(3)(B)** Non experts/expertised portion - no reasonable ground to believe that stmts in expertised portion untrue.
         1) Only really affects non-experts who knew about the expertised portions enough
      iv. Reasonableness of belief/investigation
         1) Belief: what did this person know? insider vs. outsider; level of knowledge re. biz (part of exec com?); drafted/signed reg stmt?
            a) **insider** (CEO-knows everything about the co, signed reg stmt (prospective investors reasonably assume CEO guaranteed the reg stmt's info; Director w access to info, know everything about co and its material Ks, involved in drafting the reg stmt; member of **executive committee?**);
            b) **outsider** (reas. familiar w/ biz and operations? Regularly attend bd meetings re. biz discussions? Familiar w/ co's devel of new products? Involved in co decision-making? Review drafts of reg stmt? Discuss aspects of reg stmt w/ management?). D-relying on reps of mgmt ok so long as outsider's own conduct and level of inquiry was reasonable under the circs. P arg should have probed more.
            c) "*given what____ knew about the company, his belief that the stmts were true could not have been reasonable*."
            d) Lawyers "*he may not have known about the inaccuracies but he must have appreciated some of them, given his position*"
         2) Investigation: Have to take affirmative action, look at written record, corp minutes, material Ks; can't rely on others; must independently verify
            a) **11(c)** the care required of prudent man in management of own property.

b) **Rule 176(a)-(h)** (a) type of issuer; (b) type of security; (c) type of person (CEO?); (d) office held; (e) presence of relationships to issuer; (f) reasonable reliance on officers, employees, ppl who know;
c) CEOs - even if conducted reason. invest., given position and knowledge, no way he reas. believed stmts were true.

iii) **11(a) Reliance**
i. **11(a)** if P acquired security after 1 yr of earnings statements are generally available [P purchases 1 yr after reg stmt effective]
1) P must prove reliance
2) **11(a)** Need not prove that P read the reg. stmt.-can rely on broker's reading of it

iv) **11(e) No loss causation** (reduce P's damages reward)
i. Max amount recoverable: IPO price - value of security at time of suit
ii. D tries to reduce recovery - P and D arg. disclosure dates, ct picks one (when fraud revealed)
iii. If stock went down on operative date, D arg. other reasons why stock went down: overall market drop, other neg info disclo, market irrational/overreacted/didn't understand the info. Prove other companies behaved the same. P arg. co's drop was in excess of market trends, other pos. info revealed too, companies you compare to are difft.
iv. If market didn't react: confounding events from mkt or firm (eg positive info cancels); info was leaked (already knew); mkt not efficient(mkt didn't internalize).

v) **11(b)(1),(2)** Whistleblower (issuers cant use)
i. Defendant discovers the mat'l misstmt; resigns; tells the SEC

vi) **Section 13 SOL**
i. No later than 1 year after discovery of the falsity, and no later than 3 years after the security was bona fide offered to th e public.

8. **11(e)** Damages
i) **11(g)** max damages per share is the offering price
ii) **11(e) Purchase price** (**if more than offering price, use offering price**) minus
i. **If P sold shares before suit - resale price**
ii. **If P still owns shares at end of suit - value of shares at time of filing suit**
iii. **If P sold shares after filing suit but before jmt - resale price (or value at time of filing suit, whichever greater)**
iii) Calc value of shares at time of suit - price is only good proxy for value if market knew all relevant and material info (and is efficient).
9. **11(f)(1)**, violators are jointly and severally liable
i) **11(f)(1)** contribution is allowed
i. In trial of non-settling Ds, jury assesses relative culpability of everyone, non-settling Ds must pay part that correlates to their guilt. Settling Ds don't need to pay. (Eichensholtz).
ii) Contract indemnification of U/Ws allowed
iii) **11(f)(2)** outside directors only liable in proportion to fault unless actual knowledge of misrep
iv) **11(e)** U/Ws only liable for total price they underwrite.

Section 12(a)(1) - Violation of Section 5

1. Must meet the section 13 **SOL** (no more than 1 yr from discovery of violation, no more than 3 yrs after offering)
2. **12(a) Plaintiff** is anyone purchasing a security from "seller" in violation of section 5
3. **Defendant** - (1) **actual sellers who pass title** or (2) a person who **successfully solicits** the purchase w/ motivation of own/securities owner's financial interest (gratuitous? Unpaid? Paid? Recruiting/soliciting increases worth of current project? Tip now for future one? First step to selling?)
i) **Section 15**, any control persons if no knowledge/no reasonable ground to know about liability
ii) One statutory seller can sue another statutory seller for **contribution**
4. Plaintiff must prove:
i) **The defendant violated section 5** (resale not exempt from section 5; selling before reg stmt effective; failure to deliver prospectus; made offer before reg stmt filed)
5. No causation, intent, reliance req; no showing of damages required.
6. No real defenses
i) No loss causation defense; no intent defense; no reliance defense
ii) Only real defense is to show the offering/txn qualified for an **exemption** to section 5
iii) SOL - bring w/in 1 yr from discovery of violation, no more than 3 yr from offering date
7. **12(a)** Damages
i) Rescission (give back security) if the security has not been sold: Purchase Price – Income Received
ii) Rescissionary Damages (if security already sold): Purchase Price – Sales price – Income Received

Section 12(a)(2) - Fraud in Prospectus

1. **12(a)** Plaintiff must be a person who purchased securities
i) Must have **prospectus delivery requirement** apply as to plaintiff (but need not have received; Rule 172)
2. "prospectus" is document relating to a **public offering** - can be 10(a); FWP (eg. A report); Rule 163 WKSI pre-filing stmt
3. Plaintiff must prove **material misstatement/omission in prospectus or oral stmt** as of time prosp sent out
i) When reas. investor would think fact would signif. alter the 'total mix' of info, measured as of time the reg. stmt. becomes effective
ii) Measure magnitude via % of earnings, revenue, profits; look at stock price as indicator
iii) Truth on the market defense [eg. another purchr of same secs. files suit - fraud is public]

4. **12(a)(2)** Plaintiff must not have known about its falsity
5. **Defendants** are those who offer/sell by means of the faulty prospectus
   i) Those who actually transfer title
   ii) Those who successfully solicit w/ motivation of own/securities owner's financial interest
   iii) **Under 159A**, can sue the issuer when plaintiff/purchaser purchased in initial offering from U/W in firm commitment situation
   iv) **Section 15**, any control persons of the above unless no knowledge/no reas ground to know about liability
6. **12(a)(2)** Loose reliance req - show D used a prospectus to offer securities; loose causal connection between prosp and purchasing decision (EMH)
7. No need for P to actually receive prosp;
8. No loss causation req.
9. No intent req.

10. Defendant's Arguments
   i) SOL - bring w/in 1 year from disco of fraud but and no more than 3 yrs from date of the sale.
   ii) **12(a)(2)** Plaintiff knew truth; not material
   iii) **12(b)** Absence of loss causation
      i. Max amount recoverable: IPO price - value of security at time of suit
      ii. D tries to reduce recovery - P and D arg. disclosure dates, ct picks one (when fraud revealed)
      iii. If stock went down on operative date, D arg. other reasons why stock went down: overall market drop, other neg info disclo, market irrational/overreacted/didn't understand the info. Prove other companies behaved the same. P arg. co's drop was in excess of market trends, other pos. info revealed too, companies you compare to are difft.
      iv. If market didn't react: confounding events from mkt or firm (eg positive info cancels); info was leaked (already knew); mkt not efficient (mkt didn't internalize).
   iv) **Reasonable care defense**
      i. **12(a)(2)** D can prove he did not know, and in exercise of reasonable care could not have known, of untruth/omission; won't be liable.
      ii. What did D know? level/title at co? did D exercise reasonable care? If he had, would he have known?
11. **12(a)** Damages
   i) Rescission (give back security) if the security has not been sold: Purchase Price – Income Received
   ii) Rescissionary Damages (if security already sold): Purchase Price – Sales price – Income Received

10b-5

Violate 10b-5, you violate section 10(b) of the '34 Act

1. **Jx nexus**
   i) Fraud must have occurred via means or instrumentality of ISC (write a check, use the phone, go online)
2. **Txnal nexus**
   i) Plaintiff must have **purchased/sold** a security (SEC can bring enforcement action)
      i. Note: fraud "in connection with" the purchase/sale of an investment K (an instrument that's a security) is actionable!
   ii) Defendant can be anyone whose fraudulent activity was made "in connection with" the purchase/sale of a security
3. **Material misstatement or omission**
   i) **Misstatement or Omission?**
      i. Omission when required to disclose; when necessary to make the statement as a whole true
   ii) **Materiality**
      i. Per TSC, fact is material when a **reasonable investor would think the fact would significantly alter the "total mix" of info**
      ii. **Measure materiality**
         1) **Measure magnitude via a metric** Ganino
            a) If stmt relates to 5% or more of gross earnings, revenues, income, likely material.
            b) Consider qualitative factors to put the #s into context/perspective. "*Though the misstatement related to less than 5% earnings, that particular misstatement allowed the co to (1) hide failure to meet analyst or own expectations (2) mask a change in their earnings/trends*." (arg. in Ganino) (3) change a loss into a gain (4) stmt relates to part of biz that plays a significant role in the biz's operations or profitability. Also consider (5) degree of imprecision or inherent in the statement, if it's an estimate or if it's factual. **SEC Bulletin No. 99**
            c) Is it something shhs would care about? Investors care most about income
         2) **Look at stock price change at disclosure of truth** Merck
            a) When was truth revealed on mkt?
               i) [use the facts-file reg stmt, 2 mo later, article in WSJ that reiterates info in reg stmt Merk; Food Lion]
            b) Did stock price react? Constant?
               i) **Confounding events from market or firm (offsetting pos/neg info); overall market movement; info leaked; market not efficient; market irrational; disclosure was partial. D can offer comparable company w/ PO around same t.**
            c) Explain the other drop/rise/constant on a dislo date with the above metrics.
   iii) **Truth on the market defense**
      i. If misstmt or omission already part of "total mix" in the mkt, it is not material by definition. Food Lion
   iv) **Opinions/puffery** perhaps not actionable as facts

   v) **Forward-looking statements** (eg. **21E(i)(1)** Projections of revenues etc, merger plans, stmt of future econ perf.,)
      i. To consider materiality of future event as of today, balance: **indicated probability that event will occur**; **anticipated**

magnitude of the event in light of totality of company activity
1) Probability - look at indicia of interest at highest levels such as (1) board resolutions (2) actual negotiations (3) CEO's invol.
2) Magnitude - consider (1) size of the entities involved and (2) the potential premiums over the market

ii. **Exchange Act 21E(c)(1) Forward-looking stmt SH**
1) Only **reporting issuers (21E(a)(1))** can use; Not valid during **IPOs (21E(b)(2)(D))**
2) **21E(c)(1)** fwd looking stmt not material if (1) immaterial; (2) P can't prove it was made w/ actual knowledge of falsity; (3) stmt identifying the stmt as fwd-looking and accompanied by a **meaningful cautionary statement**
a) Cautionary stmt meaningful when **discloses risks that pose the greatest possibility of undermining projections when made. Must convey substantive info about factors that realistically could cause results to differ materially from those projected**
b) No duty to update (Asher v. Baxter) but must not use same projections and cautionary stmt when know risks have changed
3) NOT REQ'D: being right about projections; being so detailed w/calculations that rivals will benefit

iii. **Oral forward-looking statements**
1) Same rule re. identify fwdlooking as such plus meaningful cautionary stmt. If mention add'l info can be found in a writing, must state you can find more info about the factors described here, and the documentation must have a meaningful cautionary stmt as well.

4. **Scienter**
i) **Intent** (to defraud), **knowledge** (that mkt will be misled), **recklessness** (conscious that stmt may be false)(Ernst & Ernst)
ii) **Pleading**
i. **21D(b)(2)** State w/ particularity for strong inference of scienter - Inference of scienter must be at least as strong as the inference of no scienter (Tellabs)
ii. Historical facts: **recklessness** or above required
iii. Fwd-looking facts: **knowledge** or above required
iii) Disco Stayed pending MTD

5. **Reliance**
i) P must prove plaintiff relied on misstmt (1) affecting decision to transact and (2) **to transact at that price**
ii) Face-to-face, prove reliance factually
iii) **Fraud on the market theory** (Basic)
i. Reliance presumed when investor buys/sells securities in reliance on integrity of the market price.
ii. P must prove:
1) **D made public misstmt; material; shares traded on efficient mkt; P traded shares between misrep made and truth revealed**. Basically, reliance on mkt price = reliance on the misrep.
iii. D can **rebut** w/ showing no link btwn mkt price/P's txn:
1) **Mkt not deceived**
a) P knew, truth entered mkt, corrective stmts made - **mkt knew truth so reliance on mkt price =/= reliance on misrep if truth was out there**
b) P can rebut this again by saying the info was **partial**; the **correction wasn't enough to fully counterbalance misstmt**
2) **P would've sold for other reasons anyway;**
3) **Mkt not efficient**
a) In order to prove a market for securities is not efficient, consider the **Cammer factors**: (a) the average weekly trading volume; (b) the number of securities analysts following and reporting on the security; (3) presence of market makers dealing with the security; (4) company's eligibility to file Form S-3; (5) cause and effect relationship between unexpected corporate news and changed in price of the security (how fast the market has reacted in the past); (6) company market cap.
iv) If can't use fraud on mkt theory, try proving reliance old-fashioned way

6. **Loss causation**
i) **Exchange Act 21D(b)(4) D's misstmt caused drop in price that caused P's damages** [use the facts: "*when the mkt found out about the fraud, price dropped. There is a **logical link between the misrep and the loss***."] if market never found out or if P re-sold before mkt found out, he will be out of luck
ii) **D rebut**:
i. **Confounding events from market or firm (offsetting pos/neg info); overall market movement; info leaked; market not efficient; market irrational; disclosure was partial. Offer evidence of other companies that did a PO at same time to compare.**
iii) **P rebut:**
i. **Drop in price was in excess of the market; mkt knew about misstmt early bc of a leak; confounding events neutralized your bad news. P argue the comparable companies are too different**

7. **Damages**
i) P entitled to out of pocket damages
ii) **K price - security's true value at time of txn**
i. True value: D argue the true value was higher than K price on day txn. Mkt knew of everything and was able to internalize but was slightly valued lower bc of market irrationality. P argue true value was much lower, a lot the mkt did not know
ii. Since this is often abstract, use rough calculation à la Dura Pharm.
iii) Rough out-of-pckt calculation: **K price - 90d average value right after disclosure of fraud** (Dura Pharm)
i. **21D(e)(1) cap for post-disclosure price volatility, 90d average will fairly impound the corrected disclo**
iv) **Exch Act 28(a)** CAP: **cannot recover more than actual damages**
i. **21D(e)(1) cap for post-txn price volatility** Damages can't exceed K price - **[90 day average of a steep drop in price]**

8. **Proportionate liability**
    i) Not joint and several

SOL is 2 yrs after disco of fraud, no more than 5 yrs after the violation

Issuer Exemptions Cheat Sheet

Issuer Exemptions: 4(2); Reg D (504, 505, 506); 3(a)(11); Rule 147

4(2)

- **Ralston Purina** - offering is nonpublic when made to people who can "fend for themselves," meaning they have both **access** to information [hold open house; offeree wealthy w/ bargaining power; hi up exec; family relationship] and **sophistication** as an investor [experience in issuers industry/biz; wealth can be proxy for sophis if lawyer up or bargaining power].
  - Number of **offerees** (not just purchasers)
  - Relationship of the offerees to each other and to the issuer
  - Number of units offered and size of the offering
  - Manner of the offering [personal contact, private - **Doran**]
- General solicitation is OK but may make an offering nonprivate
- Policy - no need to regulate here when parties don't need mandatory disclosure

Reg D

- **502(c) General solicitation**
  - Need pre-existing relationship where issuer is capable of ascertaining sophistication and financial circumstances of potential investor. In re Kenman; Mineral Lands No Action Lettr.
    - Close questions - call ppl from existing client list; talking to wealthy mutual funds, talk to golf buddies who are rich; talk to buddies from Yale
    - Need to reasonably believe sophisticated
    - "pre-existing relationship only proxy for ability to asses financial circ. and sophistication"
  - **502(c)(1)** No advertising or media/broadcast.
- **501(a) Accredited investors**
  - **(1)-(2)** various **financial institutions**; **(3)** corporations w/ assets exceeding $5M; **(4) directors, executive officers, general partners** of the issuer of the securities being offered (which includes president, VP, etc per 501(f)); **(5)** natural persons when, at time of purchase have a net worth of over $1M or **(6)** have an income of $200k individually or $300k jointly with spouse and a reasonable expectation of reaching the same income that year.
  - Issuer just needs to **reasonably believe** purchaser comes w/in this def.
- **508 Substantial compliance**
  - Mistake in Reg D offering that (1) never affected the complaining party; (2) issuer made attempt to comply; and (3) mistake insignificant wrt offering, mistake doesn't ruin application of Reg. D.
  - Significant mistakes would be: aggregate offering amount; # purchasers; no general solicitation.
- **504**
  - Not available to reporting companies
  - General solicitation OK

504(b)(2) Aggregate offering price	**1M** [consider all 504 and 505 offerings w/in one yr + offerings viol section 5]
504(b)(2) # purchasers	no limit

  - If comply with 504, offering meets 3(b) and exempt from section 5
- **505**
  - **502(c)** General solicitation not ok

505(b)(2) Aggregate offering price	**5M** [consider all 504 and 505 offerings w/in one yr + offerings viol section 5]
505(b)(2)(ii) # purchasers	any accredited; **35** non-accredited
502(b)(2) info furnish non acc	**502(b)(1)** must furnish info set out in Rule **502(b)(2)** reasonable time before sale ◆ If **reporting** co: info in public reports ◆ If **non-reporting**: non financial info + financial info (gets more strict as offering price goes up) **502(b)(2)(vii)** requires issuer to advise non-acc. investors of **resale limitations w/in reas time before sale** **502(b)(2)(iv)** requires issuer to advise non-acc investors of **any material written info given to accredited investors**.
502(d) reas care inform restricted status of secs	Take reasonable care to inform purchasers re. restricted nature of securities via **(d)(1)** inquire if purch acquiring security for investment; **(d)(2)** written disclo that restricted; **(d)(3)** legend on cert that restricted.

  - If comply with 504, offering meets 3(b) and exempt from section 5
- **506**
  - **502(c)** General solicitation not ok
  - Offering price - unlimited

Aggregate offering price	**Unlimited**
506(b)(2)(i) # purchasers	any accredited; **35** non-accredited but **506(b)(2)(ii)** non-accredited must be sophis w/ knowledge/experience to be able to evaluate merits and risks of investment
502(b)(2) info furnish non acc	**502(b)(1)** must furnish info set out in Rule **502(b)(2)** reasonable time before sale ◆ If **reporting** co: info in public reports ◆ If **non-reporting**: non financial info + financial info (gets more strict as offering price goes up) **502(b)(2)(vii)** requires issuer to advise non-acc. investors of **resale limitations w/in reas time before sale** **502(b)(2)(iv)** requires issuer to advise non-acc investors of **any material written info given to accredited investors**.
502(d) reas care inform restricted status of secs	Take reasonable care to inform purchasers re. restricted nature of securities via **(d)(1)** inquire if purch acquiring security for investment; **(d)(2)** written disclo that restricted; **(d)(3)** legend on cert that restricted.

  - If comply with 506, offering meets 4(2) and exempt from section 5

3(a)(11) Intrastate Offerings

- **3(a)(11)** securities offered/sold by local companies to local investors to finance local projects exempt from section 5.
- **Domiciled offeree-purchasers**
  - Determined by **domicile** - stay w/ intent to remain
  - Single offer to non-resident ruins; single sale to non-resident ruins. If offer to in-stater, she moves, and purchases out of state, ruins

Horizontal Integration

Safe harbors

- **502(a)** (**6mo; 12mo conclusive**) for reg D;
- **147(b)** (**6mo**) for 147 intrastate
- When you integrate, and the mega offering violates section 5, don't apply the SH, so re-do the factor test

- **Local Co.** incorporated in state & do signif income-producing biz in-state
- **Local Projects** - finance in-state projects (intent of co to use proceeds in-state is imp)
  - OK if money raised used to buy products out of state to build things in state
- **Resale**
  - Restricted securities; resident may re-sell to another resident freely
  - can only re-sell to out-of-stater after security "comes to rest" in state
  - "**come to rest**" when in-state resident **purchases security with investment intent**
    - Co will get a written document saying "I purch w/ investment intent"
- **Integration** with out-of state offering ruins this offering
- General solicitation is OK
- Available to issuers and control persons (**Rule 147 prelim note 4**)

Rule 147 Intrastate Offerings

- An offering complying w/ requirements of **Rule 147** will be exempt from section 5 under 3(a)(11).
- **Resident offeree-purchasers**
  - **147(d)(2) Residence** is principal residence @ t offer/sale; 147(d)(1)-(3) principal office (corps/pships)
  - One offer/sale to a non-resident ruins exemption
- **Local issuer**
  - **147(c)(1)(i) be incorporated in state** (corporations); 147(c)(1)(ii) location of principal office (pships); 147(c)(1)(iii) principal residence (individuals)
- **Doing business**
  - **147(c)(2)(i)** 80% of consol. **gross revenues** from operations within the state;
  - **147(c)(2)(ii)** 80% of consol. **assets** held in state;
  - **147(c)(2)(iv) principal office** located in state; **and**
- **Local financing**
  - **147(c)(2)(iii)** intent to use and does use **80% of net proceeds of offering** within state;
- **Resales**
  - Restricted securities; resident may re-sell to another resident freely; can re-sell to out of stater if "comes to rest"
  - **147(e)** SH/"come to rest" - Can re-sell to out of staters after **9 mo** from date of offering elapse
- **Precautions**
  - **147(f)** issuer must **147(f)(1)(i)** place legend on security wrt restrictions; **147(f)(1)(ii)** require transfer agent to stop transfers to out-of-staters; **147(f)(1)(iii)** obtain written representation re residence of purchasers.
- **Integration**
  - **147(b)** 6mo SH for Rule 147 offerings
- General solicitation is OK
- **Prelim note 4** Only available to issuers (not control persons)

the factor test.

- **502(a)(a)-(e)**
- **Single plan of financing**
- **Same class of securities**
- **Same time period**
- **Same type of consideration given**
- **Money raised used for same general purpose**

Consider offerings separately: Jan; Mar; Nov common stock.

1. Do any of the offerings have problems?
2. Integrate Mar into Nov? protected by SH.
   Nov into Mar? Protected by SH.
   Integrate Jan into Mar? Normally, SH applies, but b/c 3 mo apart, apply factors.
   Mar into Jan? same outcome.
3. If integrate, mega-offering violates section 5
   Lose presumption of SH, so re-do factor test
   Nov into Mar? apply factors.
   Nov. still has the SH protecting it.
4. Even if don't integrate, consider aggregation problem 504(b)(2) & 505(b)(2) (since offerings that violate section 5 count towards aggregation)
5. Re-evaluate the offerings

Burdens of Proof w/ Exemptions
Person seeking use of exemption bears burden to prove it applies
Plaintiff bears burden to rebut

Safe Harbors are not exclusive
Eg. If can't meet 147, apply 3(a)(11) or 4(2)

Resale Exemptions Cheat Sheet

Saturday, December 03, 2011
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Resale Exemptions: 4(1); 4(1 ½); Rule 144; Rule 144A

4(1) & 4(1 ½)

- **2(a)(11)** Types of U/Ws
  1) Any person who purchases securities from an issuer with a view towards distribution. [Gilligan]
     i. Incl control persons - even when acquire unrestricted shares
  2) A person who offers or sells for an issuer in connection with a distribution (professional U/W)
  3) Any person who directly or indirectly participates in the offering, selling or underwriting process for an issuer in connection with a distribution. [SEC v. Chinese Consolidated Benevolent Ass'n]
  4) Any person who purchases from a control person when such purchase is a part of the control person's distribution.
  5) A person who sells for a control person when such assistance is a part of the control person's distribution. [Wolfson]

- **2(a)(11) View towards distribution.** Gilligan
  - **View towards - 4(1)**
    - □ Investment intent (not U/W) vs. intent to resell (U/W)
    - □ Presume investment intent if investor hold for **>2yrs**
      - ◆ Plaintiff can rebut w/ facts of intent to re-sell
    - □ Conclusive investment intent if holds >**3yrs**
    - □ Presume intent to resell if hold <2 yrs, argue any facts indicating investment intent; changed investor circs. (changed issuer circs. won't work)
      - ◆ Consider: is stock his only liquid asset; is he a millionaire; was the circumstance foreseeable?
      - ◆ SEC doesn't like this
  - **Not a "distribution" - 4(1 ½)**
    - □ Made to ppl who can fend for self, sophisticated & access to info reg stmt contains
    - □ Nonpublic factors - small # offerees, relationship w/ offerees and them w/ eachother, small amount offered, manner of sale is private
    - □ Conduit approach - resale investor couldn't have participated in issuer txn [effectively helping issuer distribute to more purchasers]
    - □ Alternatively, investor can purchase now, and say, in 1 yr, give me access to info contained in reg stmt so I can give it to my resale investor; demand reg. rights agmt
    - □ General solicitation or wide distribution may ruin this
    - □ Selling to Nasdaq is def. a distribution bc selling to lots and lots of ppl

- **2(a)(11) Participates.** Chinese Consol. Benev. Ass'n
  - Person who participates in issuer's distribution for **benefit of issuer**
  - Consider extent of help and involvement: Continually solicit; hype securities to help issuer
    - □ "soliciting is the first step to sell"
  - Participant need not be paid, no K need exist, issuer need not know participant's existence

- **2(a)(11) Purchase or sell for a control person in a distribution**
  - **2(a)(11)**, control person considered issuer wrt defining U/W
    - □ Broker; resale investor
  - Argue not a "distribution" under 4(1 ½)

- If not U/W, can use 4(1) exempt the txn
- **Resale** under 4(1) & 4(1 ½) is a transfer of **restricted** securities
  - ○ Continue to be restricted until (1) register the securities; (2) sell under 144; (3) "come to rest" (4(1) - hold for 3 yrs [conclusive]); 3(a)(11) "purch w. investment intent"; 147 free to re -sell after 9mo of offering)
  - ○ No holding period to use 4(1) & 4(1 ½)
  - ○ Tack holding periods for purposes of "coming to rest" under 4(1) & 4(1 ½)? Policy
    - □ If inequality of info is more imp., allow tacking because, have info available in market now
    - □ If investment intent is more imp., don't let tack because want them to hold for long t

- If deemed U/W, must **vertically integrate**; does new integrated txn fit under any exemption?

Control Persons & Affiliates 144(a)(1)
Considered issuers under 2(a)(11)
A person with "control" per 405, meaning person w/ power to direct the management and policies of issuer whether by ownership of voting rights, by K, or otherwise.
% stock ownership
Director? "he's on the Bd, decide co matters, access to info, power to control decisions"
Officer?
Power to:
Control mgmt and policies of issuer
Compel issuer to obtain signatures nec. to file a reg. stmt.
Access to good info, constant

Rule 144

- If comply with requirements of Rule 144, investor or affiliate won't be an U/W for the issuer; person helping affiliate won't be U/W of affiliate; purchaser from affiliate won't be an U/W for affiliate b/c not a "distribution"
- **Rule 144 preliminary note** Securities received are "**cleansed**"
  - ○ If Rule 144 is perfected, securities acquired are cleansed, can be freely re -sold willy nilly

- **144(a)(1) Affiliate** of issuer is person who directly/indirectly controls the issuer (control per Rule 405)
  - ○ (1) **officer** of issuer; (2) **director** of issuer; (3) shareholder with **10% or more**
  - ○ Consider relationship w/ insiders
  - ○ (1) Power to direct/control the management/policies of issuer via shh voting rights, by K, etc. (2) power to compel issuer to file reg stmt covering the control person's securities.

- **144(a)(3)** restricted securities those attained from (1) nonpub offering; (2) Reg D. (3) 144A

- **General Requirements 144(b)(1),(2)**
  - **144(d) Holding Period**
    - Holding period runs from date of purchase from **issuer** or **affiliate**, **whichever is later**.
    - Holding period re-sets when purchase from an issuer or from an affiliate
    - Can tack holding period times when purchase from non-affiliate

Reporting Co	**6mo** (restricted only) Affiliate & non
Non-reporting Co	**1 yr** (restricted only) Affiliate & non
	Unrestricted security **ZERO** holding period (mostly when CP acq. unrestr. shares)

  - **144(c) Current Public Information**

	Non-Affiliate	Affiliate
Reporting ***current w/Exchange Act reporting reqs for 12mo**	1 yr from issuer txn **144(b)(1)(i)**	Always
Non-reporting ***provide info listed in Rule 15c2-11**	No info req. **144(b)(1)(ii)**	Always

    - **144(c)** reporting companies fulfill info req. by being current on Exch Act reporting reqs for 12mo. Non-reporting companies fulfill info req by making available info listed in 15c2-11

- **Affiliates Only 144(b)(2)**
  - **144(e) Volume Limit**
    - **144(e)(1) amt securities sold right now** + **all sales of same class of securities in last 3 mo** can't exceed greater of:
      - 1% of shares of class outstanding or
      - Average weekly reported trading volume of the past 4 weeks
    - Sales of same class of securities in last 3 mo includes: registered & unregistered securities but not:
      - 144(e)(3)(vii) securities they registered & sold (not to be confused w/ buying secs in PO and re-selling them); securities sold in txn exempt under 4(1) and 4(1½) that were "private"
  - **144(f),(g) Manner of Sale**
    - **144(f)** affiliate must sell securities in unsolicited brokers' txn per 4(4) and defined in **144(g)**
    - **144(g)(1) broker simply executes orders**
    - **144(g)(2) can't pay broker more than customary commission**
    - **144(g)(3) Can't solicit or arrange for solicitation**
  - **144(h) Notice Requirement**
    - **144(h)** must file Form 144 with SEC if sales of secs in 3mo period exceed 5,000shares or $50,000.

- Can re-sell restricted shares via an unsolicited broker txn on the Nasdaq [so long as holding period met, info req met, volume limit met, notice given]
- If Rule 144 not met, still argue 4(1) or 4(1 ½)

Rule 144A

- 144A if comply with requirements in Rule 144A, resale of restricted securities to QIBs is not a "distribution" such that reseller can benefit from 4(1)

- **144A(a)(1) QIBs**
  - Entities in the biz of investing as enumerated in 144A(a)(1)(i): insurance co, investment co, employee benefits plans, dealers, mutual funds, banks (with $100M in securities and net worth of $25M)
  - Individuals cannot be QIBs
  - Seller must reas. believe purchaser is QIB
- **144A(d)(3) Fungibility**
  - **144A(d)(3)** can't sell securities under this rule that are of same class as securities listed on nat'l exch
  - Securities that are convertible may be ok so long as there's restrictions on conversion
- **144A(d)(2) Notify purchaser**
  - **144A(d)(2)** Seller take **reasonable steps** to notify QIB that txn is under 144A and unregistered
  - Can place legend on securities indicating restricted status; include stmts in private placement memo to make it clear
- **144A(d)(4) Disclosure of Info for non-reporting issuers**
  - **144A(d)(4) non-reporting** issuers, **upon request from purchaser**, must provide certain 'reasonably current' basic info concerning the issuers' biz, products, show balance sheet and financial statements from past 2yr.

- **144A prelim note** securities acquired are **still restricted**

- No holding period
- Seller can **generally solicit** QIBs
  - "the fact that investor generally solicited the QIBs does not affect the 506 transaction"
- If 144A not met, argue Rule 144 or 4(1) & 4(1 ½)