

## **Dissemination of Information During the Initial Public Offering Process**

### **Overview**

Companies engaged in the IPO process are limited in their ability to communicate with outsiders or the media. Section 5 of the Securities Act prohibits a company from making written offers to sell its common stock in an IPO until a registration statement that includes a prospectus with a price range is on file, and prohibits sales of the common stock until the registration statement is declared effective by the SEC. The SEC considers a wide range of communications to constitute selling efforts or an “offer” to sell securities. For example, the SEC may consider statements regarding the growth of the company or its industry to be impermissible conditioning of the market.

“Gun-jumping,” a common term for making offers before offers are permitted, can have a number of negative consequences for a company and its offering. These consequences can include (i) strict liability for statements that may not have been adequately vetted through the diligence process, (ii) an SEC-imposed “cooling off” period that could delay the IPO, or (iii) potential violation of Section 5 of the Securities Act, which can result in rescission rights for purchasers of the shares.

A company should begin to take care regarding its communications when it begins the IPO process, no later than the time at which the company has engaged its underwriters. Even before that time, however, company executives should avoid any public statements or discussions about a potential IPO. Any mention of an offering will result in the unavailability of most safe harbors, so it is of primary importance that companies avoid discussion of the potential offering in all communications. This quiet period continues through the consummation of the offering, until 25 days after the date of offering, after which time dealers are no longer required to deliver a prospectus in connection with sales of the shares.

In general, companies are permitted to continue to communicate about their business and products in the ordinary course of business, consistent with their past practice. However, the restrictions regarding gun-jumping involve a combination of rules, practice and judgment, so companies engaged in the IPO process should consult early on with counsel regarding their communications practice and policies. Generally communications (including press releases, interview plans and conferences) during the IPO process will be reviewed by both the company’s and the underwriters’ counsel before release, even if they are expected to be permissible.

## *Generally Permissible Communications*

- Normal advertising of products and services, if consistent with past practice.
- Dissemination of regularly released factual information to non-investors (i.e. customers and suppliers) regarding business and financial developments unrelated to the IPO, if consistent with past practice.
- Participation in trade shows and industry meetings and publication of articles in the trade press, if consistent with past practice.
- Responses to inquiries regarding factual matters (unrelated to the IPO or the company's prospects), if consistent with past practice.
- Announcements to the media with respect to factual business and financial developments (unrelated to the IPO or the company's prospects), if consistent with past practice.

## *Generally Prohibited Communications*

- New or significantly expanded advertising campaigns related to corporate branding. The SEC may view these as attempts to condition the market, and thus prohibited communications.
- Statements or forecasts regarding the company's revenues, income or growth prospects, or regarding industry growth prospects. Even statements such as "We expect to continue to grow" should be avoided.
- Discussions with the media or public announcements regarding the IPO or the company's business strategy, financial performance or general prospects.
- Discussions with securities analysts regarding the company or the IPO (except in connection with the due diligence process or pursuant to a non-disclosure agreement).
- Participation in investor or analyst conferences, except as conducted with the underwriters in the road show.
- Advertisements of the common stock.

The same rules apply to digital communications as to traditional forms of communication, and companies should subject their websites, digital advertising, social media presence and other digital communications to the same level of scrutiny.

## *Recommended Policies*

Given the sensitivity of disclosure during the IPO process and the potential liability or delay an inappropriate disclosure may cause, companies should establish the following policies in order to avoid potential problems:

- One or two senior officers should be designated to respond to all contacts by investors and the media.
- Companies should limit communications to factual matters, continue to conduct their business affairs in the customary manner, consistent with past practice, and try to avoid or limit dealings with the press.
- Detailed records of all press releases, speeches, presentations, advertising and other communications should be retained to show that there has been no increase in frequency or change in content in connection with the IPO.
- Counsel should review all public communications prior to their release.
- Counsel should preclear any media interview, conference presentation or other public speaking request.
- Companies should not increase their Internet presence.
- Companies should adopt a policy prohibiting employees from posting company information online (including on personal social media sites, in online discussions and in chat rooms).
- Companies should ensure that their directors and senior management in particular understand the limitations on communications during the IPO process.
- Companies should be mindful that even with information security policies in place, internal communications may be leaked to the media. Depending on their contents, leaks can create liability and cause delays.

## *Limited Exceptions*

While companies and their representatives should generally avoid all communications about the IPO and the company's growth and prospects as discussed above, the securities laws provide some exceptions under which some communications are permitted in certain circumstances.

However, such exceptions are limited in scope and, consequently, utility. Companies should rely on these exceptions only with the guidance of counsel.

## Regularly Released Factual Business Information

Securities Act Rule 169 provides a non-exclusive safe harbor for communications of factual business information. Factual business information includes factual information about the issuer, its business or financial developments, or other aspects of its business and advertisements of, or other information about, the issuer's products and services. This rule does not cover forward-looking information, only historical information. To qualify for the safe harbor of Rule 169:

- The issuer must have previously released or disseminated information of the type described in the rule in the ordinary course of its business.
- The timing, manner and form in which the information is released must be consistent in all material respects with similar past releases or disseminations.
- The information must be intended for use by persons, such as customers and suppliers, other than in their capacity as investors or potential investors.
- The information must be released by the issuer's employees and agents who historically have provided such information.

Any communication relying on this rule must not contain any information about the offering.

## *Communications More Than 30 Days Before Filing*

Securities Act Rule 163A creates a safe harbor period, ending 30 days prior to the public filing of a registration statement, during which most communications are deemed not to be "offers." For purposes of this rule and other communications rules, "filing" refers to the public filing of a registration statement, and not a confidential submission under the JOBS Act. The availability of this safe harbor is subject to conditions:

- The communication must not reference the IPO.
- The communication must be made by the company or authorized by a representative of the company (other than an underwriter or dealer).
- The company must take reasonable steps to prevent distribution or publication during the 30-day period immediately prior to the public filing of the registration statement. (This can be a trap for the unwary. An interview given more than 30 days before filing, but published less than 30 days before filing, could be a prohibited communication.)

## *Limited Content Notices*

Securities Act Rules 134 and 135 provide safe harbors by which a company may issue a press release containing certain information about an IPO. However, these safe harbors are narrow in scope and consequently seldom used except in special circumstances (for instance, a company might release a

limited content notice if it believes that a press release will be necessary to bring the IPO to the attention of customers or suppliers). Rule 135 permits a company to give notice before filing a registration statement that it proposes to make a public offering, while Rule 134 permits a company to publish very limited advertisements of a security after the registration statement is publicly filed. Only basic information, such as the company's name and the terms of the security, may be released under these rules.

## *Oral Offers*

After the registration statement is filed publicly, a company can make oral (as opposed to written) offers to sell. However, under the SEC's interpretation, almost all communications are considered "written," including broadcasts, most electronic communications and broadly disseminated or "blast" voicemail messages. Only certain real-time oral communications qualify as "oral" under the SEC's interpretation. For instance, an individual voicemail message originating in a live telephone call would be an oral communication. Presentations that involve real-time communication to live audiences, including via webcast, are oral offers as well. Webcasts accessible on demand, on the other hand, are written offers. Because the definition of "oral" offers is so narrow, companies generally avoid making any offers, oral or written, until written offers are permitted.

## *Written Offering Materials*

When the SEC review process is almost complete and the prospectus has been amended to include the estimated price range for the common stock (this version of the prospectus is known as the "statutory prospectus"), a company may use the statutory prospectus to make offers. A company also may use other written communications, known as "free writing prospectuses" or "FWPs" to make offers, but only if the statutory prospectus accompanies or has preceded each such FWP. Accordingly, broad dissemination of an FWP is not usually feasible except (i) in an electronic form containing an active hyperlink to the statutory prospectus or (ii) to potential investors known to have received the most recent statutory prospectus. Examples of FWPs include e-mails, faxes, Website posts, on-demand webcasts and blast voicemail messages.

FWPs generally must be filed with the SEC at the time they are used. FWPs are treated as prospectuses under the federal securities laws, and accordingly carry the same risk of liability as information in the statutory prospectus. Because they may only be used in these limited circumstances, FWPs are primarily used to communicate any necessary updates during a roadshow. All FWPs should be cleared with counsel first to ensure they contain any requisite legends and do not contain prohibited information, and so that the underwriters for the offering can be made aware of the intended use of an FWP.

## *Publicity*

As discussed above, companies should generally avoid communicating with the media during the IPO process except with regard to factual business matters in a manner consistent with past practice. Company representatives should not comment on the IPO under any circumstances.

The rules regarding FWP do offer some protection from violations of Section 5 of the Securities Act as a result of media stories, but the company may still take on securities liability for the content of those stories. If a company has participated in a media communication, for example by granting an interview, any resulting news story could constitute an FWP when published (referred to as a “media FWP”). Unlike other FWPs, a media FWP does not have to be preceded by a statutory prospectus. However, if a media communication is an FWP, the company must file the media communication with the SEC unless the substance of the communication has previously been filed with the SEC. Whether or not filed, any media FWP is treated as a prospectus under the federal securities laws, and therefore could result in liability for any material misstatements or omissions.

It is important to note that a company may not pay for media publicity or otherwise solicit such publicity, as it would be required to deliver a statutory prospectus in advance of or along with such coverage. As this is generally impracticable, companies should avoid this practice.

### *Testing the Waters*

Pursuant to the JOBS Act, adopted in 2012, an emerging growth company (or “EGC”) may engage in written and oral communications to institutions that are “qualified institutional buyers” or “accredited investors” at any time before or after the filing of a registration statement. The use of this practice, referred to as “testing the waters” is growing. An issuer can expect the SEC to request copies of any written materials used in testing the waters activities. Companies should consult with counsel and, if engaged, underwriters, before engaging in any testing the waters activity.

### *Conclusion*

While the quiet period associated with an IPO can be challenging, with care and input from counsel, a company should be able to communicate with its customers, suppliers and other constituents in a way that does not seriously inhibit its business or its sales and marketing efforts while still not adding any material risk to the IPO process.

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