

CLIENT ALERT

SEC Extends “Testing the Waters” Exemption to All Companies

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The Securities and Exchange Commission recently issued final regulations permitting all companies to “test the waters” regarding certain investors’ potential interest in a securities offering.¹ New Rule 163B, which extends the exemption currently available only to emerging growth companies (“EGCs”), permits issuers to engage in oral or written communications with certain sophisticated institutional investors, either prior to or following the filing of a registration statement, to determine whether such investors might have an interest in a contemplated registered securities offering. The rule is designed to facilitate access to the public markets by allowing issuers to gauge investor interest without incurring the significant costs associated with preparing and filing a registration statement. The regulations become effective on December 3, 2019.

Investor Status

Rule 163B permits an issuer to engage in pre- and post-filing solicitations of interest with potential investors that are, or that the issuer reasonably believes to be, Qualified Institutional Buyers (“QIBs”) or Institutional Accredited Investors (“IAIs”). A QIB generally is a specified institution that, acting for its own account or the accounts of other QIBs, in the aggregate, owns and invests on a discretionary basis at least \$100 million in securities of unaffiliated issuers. An IAI is any institutional investor that is also an accredited investor, as defined in paragraph (a) of Rule 501 of Regulation D.² Under the rule, any potential investor solicited must meet, or the issuer must reasonably believe that the potential investor meets, these requirements.

¹ See SEC Release No. 33-10699, *Solicitations of Interest Prior to a Registered Public Offering*, available [here](#).

² An institutional investor that meets the criteria of Rule 501(a)(1), (a)(2), (a)(3), (a)(7) or (a)(8) of Regulation D.

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Availability of Exemption for Underwriters

In extending the availability of the testing the waters exemption to all issuers, Rule 163B also permits underwriters to communicate with potential investors prior to the filing of a registration statement, provided they are authorized to do so by the issuer. Current Rule 163 only applies to “well-known seasoned issuers” (“WKSIs”), and does not extend to the underwriters of a WKSIs offering.

Not a Free Writing Prospectus; No Filing Requirement; Regulation FD

The rule exempts qualifying testing the waters communications from the definition of free writing prospectus under Rule 405 and the prospectus filing requirements under Rule 424(b). However, any such communications are considered offers under the Securities Act and as such remain subject to the anti-fraud provisions under the federal securities laws, including Section 12(a)(2) under the Securities Act. The SEC notes that, even though there is no filing requirement, the staff may request copies of any testing the waters communications in connection with its review of a registration statement, similar to its current practice with respect to EGCs. In making Rule 163B communications, issuers would need to make sure they comply with the selective disclosure rules of Regulation FD.

Non-Exclusivity

Under the non-exclusive exemption provided by Rule 163B, an issuer would be able to rely concurrently on other Securities Act communications exemptions when determining how, when and what to communicate in connection with a contemplated securities offering. However, the SEC cautions that an issuer that solicited interest from QIBs and IAs in reliance on Rule 163B would need to make sure it had not engaged in a general solicitation were it to rely on a private placement exemption in lieu of proceeding with a registered offering.

Use by Registered Investment Companies and BDCs

The exemption provided under Rule 163B similarly applies to issuers that are, or that are considering becoming, registered investment companies or business development companies (“BDCs”). The SEC noted, however, that legal and other considerations (including the need to comply with Investment Company Act registration requirements) would likely limit the use of Rule 163B to BDCs and certain closed-end funds.

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If you have any questions regarding this client alert, please contact the following attorney or the Willkie attorney with whom you regularly work.

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