INSIGHTS

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SECURITIES OFFERINGS

Term Sheets and Other Communications after Securities Offering Reform

The SEC's recent securities offering reforms have led to renewed focus on methods of conveying preliminary and final terms in institutional fixed income offerings. The means by which this information has been conveyed also presents a viable alternative for conveying information prior to the time of contract of sale in registered offerings of virtually every category of securities.

by Bruce C. Bennett and Sean G. McAuliffe

Fixed income syndicate desks historically have used a variety of approaches to convey pricing and other information regarding debt and convertible securities [1] to institutional investors. A common means of confirming final pricing terms to institutional investors has been a subscription-based email system maintained by Bloomberg LLP. These emails are generally referred to as "Bloomberg screens." Typically, shortly after pricing, the syndicate desk will prepare a summary term sheet containing basic terms of the just-priced security. It then forwards this screen to members of the investment bank sales force who were involved in the offering. These salespeople, in turn, transmit the screen to customers who have received allocations in the offering.

The SEC's recently-adopted securities offering reforms[2] affect the use of Bloomberg screens as a means to convey preliminary and final terms of fixed income securities to institutional investors. The reforms have also created concerns in the eyes of certain market participants with the market practice of delivering Bloomberg screens promptly following pricing. As described subsequently, the rules relating to free writing prospectuses address these concerns by providing a means for underwriters to continue to deliver final term sheet screens to their accounts in the moments after pricing while also permitting issuers to take liability on a version of the document that they have had a meaningful opportunity to review.

Bloomberg screens have also emerged as a viable means of conveying material information to institutional investors prior to the time of contract of sale in offerings of virtually every category of securities. This functionality presents an additional option for practitioners seeking to comply with the SEC's liability interpretation under the offering reforms and new Rule 159 under the Securities Act of 1933 (Securities Act).[3]

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How Do Underwriters Use Bloomberg Screens?

At the pricing of an institutional fixed income transaction, the syndicate desk generally prepares a Bloomberg screen containing final terms of the security. This screen is often a single screen in length, although the Bloomberg system can accommodate much longer transmissions. The screen will include, typically in highly abbreviated form, final terms of the just-priced security. By way of example, a post-pricing screen might contain the following hypothetical information:

FINAL PRICING TERMS

Widget Industries, Inc. Convertible Senior Subordinated Notes Due 2018

SIZE: $350MM PLUS: $35MM SHOE
MATURITY: 11/30/18 PAR AMT: $1,000
TICKER: WGT / NYSE
COUPON: 4.75% through 11/20/10; 5.25% thereafter
PREMIUM: 22.00% LAST SALE: $21.19
CONVERSION PRICE: $25.85

CONVERSION RATIO: 38.6820
T/D: 11/18/05 S/D: 11/23/05

FIRST COUPON: 5/31/06
CALL: November 30, 2010 at par

CUSIP: 12345XXX5
PUTS: November 30, 2010 at par

GROSS SPREAD: $25.00 SELLING: $15.00
MGMT: $5.00 U/W: $5.00

BOOKRUNNER(S): ABC INVESTMENT BANK
SPLITS: 42.5/42.5/15

CO MANAGER(S): None

EXPECTED RATINGS: B3/B (Moody's/S&P)

A screen is prepared in the moments immediately following pricing and is then forwarded to internal salespeople involved in marketing the deal. These salespeople, in turn, forward the screen to each customer who received an allocation in the offering. Historically, these screens have been used without prior review by outside counsel for the issuer or the underwriter. In-house counsel at the investment bank may review a post-pricing screen, but any such review would not delay the transmission of the screen to the institutional investors.

The post-pricing screen is not intended to serve as a formal confirmation meeting the requirements of Rule 10b-10 under the Securities Exchange Act of 1934 (Exchange Act), but instead is used to confirm to the investor the basic terms on which it received an allocation in the offering. A Rule 10b-10 confirmation is then prepared and delivered prior to the closing of the transaction.[4]

In an offering with multiple underwriters, each firm will typically prepare its own version of a post-pricing Bloomberg screen, although in certain circumstances a bookrunner will prepare the screen and forward it to other syndicate members for their use.

In addition, Bloomberg screens are often prepared earlier in an offering as a means of communicating with prospective institutional investors. For example, a screen can be prepared at the time of the launch of the offering. Such a screen may contain proposed terms of the security (sometimes with indicative pricing, expressed as a range), and may also contain anticipated timing. These screens would again be prepared by syndicate, forwarded to sales and used by sales to introduce prospective institutional accounts to the offering. If there is a material change in proposed terms or timing, a new Bloomberg screen can be created and distributed to update institutional investors. Finally, certain Bloomberg screens can be accompanied by attachments. It is thus possible, for example, to attach a base prospectus, form of indenture or other document to a Bloomberg communication.

Analysis of Bloomberg Screens under the Securities Act

Rule 134

Rule 134 under the Securities Act, which was revised as part of the offering reforms but was initially adopted in 1955, provides a safe harbor from the gun-jumping provisions of the Securities Act for limited

public notices about a registered offering.[5] Rule 134 could be relied on for certain Bloomberg screens if content and legending restrictions are complied with and, in the case of pre-pricing screens, a registration statement containing a statutory prospectus relating to the offering has been filed prior to the transmission of the screen. Content restrictions imposed by Rule 134 would generally limit the ability to rely on this rule to communications regarding the most straightforward debt securities (typically straight debt with no put, call or Treasury make-whole provisions). In addition, in both of the Offering Reform Releases, the SEC stated that Rule 134 could not be used to provide a detailed description of securities being offered.[6]

Free Writing Prospectuses

A Bloomberg screen used to offer securities or convey final terms that fall outside the scope of Rule 134 would constitute a free writing prospectus under Rule 405 of the Securities Act.[7] The treatment of such a screen under the offering reforms will vary depending on the timing and content of the screen.

Post-Pricing Term Sheet Screens. Bloomberg screens issued after pricing that describe the final terms of the offered securities must be filed by the issuer within two days of the later of the date such final terms have been established and the date of first use, regardless of whether it was prepared by or on behalf of the issuer or another offering participant.[8] In most instances, first use will occur on the date that final terms are established. The screen must contain the legend required by Rule 433(c)(2)(i) of the Securities Act.[9] To the extent these screens are filed with the SEC, they are not otherwise required to be retained by the underwriter that created them. Any screen that is a free writing prospectus will be subject to disclosure and anti-fraud liability under the Federal securities laws (Sections 12(a)(2) and 17(a)(2) under the Securities Act and Rule 10b-5 under the Exchange Act).

Historically, Bloomberg final term sheets have been prepared and transmitted within moments of pricing, without issuer or outside counsel review.

Pre-Pricing Term Sheet Screens. A Bloomberg screen transmitted by an underwriter prior to pricing that contains preliminary terms of the offered securities is not required to be filed with the SEC.[10] Any such screen must be retained by each underwriter that used it for three years following the initial *bona fide* offering of the securities in question,[11] must contain the legend required by Rule 433(c)(2)(i) and will be subject to disclosure and anti-fraud liability under the Federal securities laws.

Underwriter-Generated Screens Containing Information Beyond Preliminary or Final Terms. Underwriters occasionally include in Bloomberg term sheet screens additional market or other information regarding the offering. For example, information regarding yield to maturity, comparisons of yield or other terms to comparable recently-issued securities or other metrics could be included. Additional information such as this would not generally constitute "issuer information" as defined in the offering reforms.[12] Therefore, inclusion of this additional information would not require an otherwise non-fileable pre-pricing Bloomberg screen containing preliminary terms to be filed by the issuer with the SEC.

As an underwriter free writing prospectus, the screen also would not be required to be filed with the SEC by the underwriter that used it unless the screen was used or referred to by the underwriter, or distributed on behalf of such underwriter, in "a manner reasonably designed to lead to its broad unrestricted dissemination."[13] Bloomberg screens are only available to specified recipients, each of whom must be a subscriber to the Bloomberg system. Although the question of whether a communication was disseminated in a broad, unrestricted manner is a facts and circumstances determination, it would appear that the subscription-based structure of the Bloomberg system and the relatively high cost of subscription would cause Bloomberg screens not to meet this "unrestricted dissemination" test. If this were to be the case, then an underwriter free writing prospectus transmitted via the Bloomberg system would not be required to be filed by the underwriter with the SEC.

These underwriter-generated screens would be subject to the legending, record retention and disclosure and anti-fraud liability provisions already discussed.

Issues with Bloomberg Screens under Securities Offering Reform

Accommodating Market Practice in Delivering Bloomberg Screens

A final term sheet is a free writing prospectus that must be filed by the issuer. Historically, Bloomberg final term sheets have been prepared and transmitted within moments of pricing, without issuer or outside counsel review. In instances since the effective date of the offering reforms when a post-pricing screen has been delayed to permit such a review, institutional investors have often presumed that something has gone wrong in the pricing of the deal. This can create risk that investors that had committed to the offering will reconsider their decision when in fact there is no reason to do so.

These facts have created tension in certain institutional fixed income offerings since the effective date of the offering reforms. Issuers, on the one hand, understandably are interested in the content of any free writing prospectus that they will be required to file and on which they will take liability. Underwriters, on the other hand, are anxious to avoid delays in delivering to their clients post-pricing communications that have become a standard part of institutional fixed income transactions.

The offering reforms provide a means to resolve this potential dilemma. As noted, a free writing prospectus that contains only a description of the final terms of an issuer's securities or of the offering shall be filed by the issuer with the SEC within two calendar days of pricing. Rule 433(d)(4), which was adopted as part of the offering reforms, provides:

> The condition to file issuer information contained in a free writing prospectus of an offering participant other than the issuer shall not apply if such information is included (including through incorporation by reference) in a prospectus or free writing prospectus previously filed that relates to the offering.

If an underwriter creates a final term sheet Bloomberg screen and transmits it to its accounts immediately after pricing, there are two alternative means by which the SEC filing obligation thus created can be satisfied. First, the issuer can file the version of the screen created by the underwriter under Rule 433(d)(5)(ii) within two calendar days of pricing. Second, the issuer can create its own version of the final term sheet and file that version with the SEC under Rule 433(d)(5)(ii) within the same two calendar day time limit. If the issuer creates and timely files its own version of the final term sheet, the underwriter's earlier version is not required to be filed as the issuer has already filed the issuer information relating to the offering, and thus under Rule 433(d)(4) a second filing of the same information is not required.

What does this two-step approach accomplish? Perhaps most importantly, it permits the issuer to take ownership of the form and content of a final term sheet free writing prospectus without having to insert itself or its outside counsel in a review of the underwriter's version in the moments after pricing. At the same time, this approach permits the underwriter to continue prior practice of delivering this information in the time frame that the market expects to receive it. While it is theoretically possible for an issuer or its outside counsel to pre-review a form of final term sheet Bloomberg screen prior to pricing without unduly delaying its transmission, in practice these reviews have often taken hours, if not more than a day, creating the unnecessary concern in the market as to whether a problem has arisen with the deal.[14]

Moreover, if an underwriter inadvertently misstates a term in its Bloomberg screen, that does not necessarily create liability for the issuer. Assuming that the error is corrected in the issuer's version that is filed, the underwriter's variant becomes a non-final term sheet, which is not required to be filed by the underwriter with the SEC. In addition, the incorrect term is not issuer information as defined in Rule 433, and thus is not required to be filed by the issuer. In such a situation, the underwriter that distributed the incorrect information would have to determine whether, and if so, how, to convey corrected information to its accounts.

If an underwriter elected to include in its version of the Bloomberg screen market information in addition to final terms, that also would not create a separate filing obligation or additional liability for the issuer. As noted, this market information would not constitute issuer information and thus would not

be required to be filed by the issuer. In addition, since use of the Bloomberg system would not constitute broad, unrestricted dissemination, the underwriter would not be required to file the screen.

If this approach is followed, the screen prepared by the underwriter would be subject to the record retention requirement for free writing prospectuses, since that screen would not have been filed with the SEC. In addition, Rule 433's legending requirements and Federal securities law disclosure and anti-fraud liability would apply.

Content Concerns

Free writing prospectuses are not subject to specific line-item disclosure requirements or otherwise required to contain specified information (other than the legend mandated by Rule 433) or to follow a specified form. Instead, the offering reforms provide that free writing prospectuses must not conflict with information contained in the registration statement or periodic reports that are incorporated by reference therein.[15] As noted, free writing prospectuses are subject to disclosure and anti-fraud liability under the Federal securities laws.

Despite the latitude afforded by the offering reforms as to scope and content of free writing prospectuses, there have been objections to final term sheets proposed to be disseminated by offering participants in certain transactions that may not be warranted. For example, Bloomberg term sheets typically are highly abbreviated. This is consistent with custom and practice in this area, and also with investors' expectations. Thus, it is not necessary to recast a term sheet into full sentences, or recast well known acronyms into full words, solely because the screen will constitute a free writing prospectus.

Free writing prospectuses are subject to disclosure and anti-fraud liability under the Federal securities laws.

In addition, term sheets generated by underwriters typically only contain terms that are viewed by market participants to be material. It is not necessary for the term sheet to contain every term of the security in question. For example, record dates for interest payments are included in the terms of all fixed income securities. However, in a world where virtually all debt securities are held in book-entry form, this term is relevant only in extremely isolated circumstances. The omission of such a term from a Bloomberg final term sheet should not give rise to concerns as to the adequacy of disclosure contained therein.

Legending Requirements

Any free writing prospectus must contain the legend mandated by Rule 433.[16] In addition, the Offering Reform Releases identify a series of legends and disclaimers that are not permitted in free writing prospectuses. Included among these are legends to the effect that the communication is neither a prospectus nor an offer to sell or a solicitation of an offer to buy.[17] Industry practice prior to the effective date of the offering reforms was that each firm would include its own version of a generic legend that was automatically inserted by the Bloomberg system on every Bloomberg screen transmitted by that firm. Most versions of these legends contained "no offer" language that is not permitted to be included in free writing prospectuses. The industry, working with Bloomberg, has modified their procedures such that Bloomberg screens that constitute free writing prospectuses contain the mandated Rule 433 legend and no longer contain the impermissible "no offer" language.[18]

Retention Requirements

Any free writing prospectus that is not filed with the SEC must be retained by the underwriter that used it for three years following the initial *bona fide* offering of the securities referenced therein.[19] Bloomberg redelivers to its clients on a daily basis all emails sent over the Bloomberg system to facilitate compliance with existing record retention requirements. Free writing prospectuses sent via the Bloomberg system are thus part of this redelivery. Bloomberg has developed the capacity to separately redeliver screens carrying Rule 433 legends to ease compliance with the new retention requirements imposed by Rule 433.

Treatment of Bloomberg Screens in Underwriting Documents

The use of Bloomberg screens as a means to communicate with investors raises questions as to

how these communications are addressed, if at all, in underwriting agreements.[20]

Rule 134 communications do not constitute a prospectus for purposes of Section 2(a)(10) of the Securities Act or a free writing prospectus for purposes of Rule 405 thereunder. Therefore, to the extent that a Bloomberg screen is treated as a Rule 134 communication, it could be excluded from the issuer's representations and warranties regarding accuracy of disclosure, the issuer's indemnity and counsels' negative assurance letters. This is consistent with long-standing practice for Rule 134 communications.

Bloomberg screens also present a means by which to convey material information to such investors prior to the time of contract of sale.

To the extent that a Bloomberg screen constitutes a free writing prospectus, it carries disclosure and anti-fraud liability under the Federal securities laws whether or not it is filed with the SEC. Therefore, it is reasonable to expect that underwriters may seek to include the substance of free writing prospectuses among the disclosures to which the issuer's representations and indemnity and outside counsels' negative assurance letters apply. If this approach were to be followed in a particular offering, the issuer's representations and warranties with respect to disclosure, the issuer's indemnity and outside counsels' negative assurance letters would cover the substance of these screens. If the approach to post-pricing term sheet screens described previously is adopted such that the issuer files its own version of a post-pricing Bloomberg screen term sheet to obviate the need to file the underwriter's version pursuant to Rule 433(d)(4), the issuer's, but not the underwriter's, version would be part of the disclosure package. Therefore, so long as the information in the underwriter's version accurately reflected the final terms of the security, the same information will be in the issuer's version and thus the underwriters will receive the same degree of coverage in terms of representations, indemnification and negative assurance opinions.

In the days leading up to the effectiveness of the offering reforms, certain issuers adopted a view that there should be no use of free writing prospectuses other than to correct errors contained in previously-issued prospectuses or to update for unanticipated material developments. Certain issuers were also inclined to require that any free writing prospectus be approved by the issuer or its counsel in advance of use. Although these approaches have not become standard practice under the offering reforms, they still do arise from time to time. These limitations would impair the ability of underwriters to continue to use Bloomberg screens in institutional fixed income transactions.[21] The Securities Industry Association recently published a memorandum of possible changes to contractual underwriting provisions in light of the advent of offering reform, which includes language that would permit the use of Bloomberg screens without prior issuer consent.[22]

Finally, any market information contained in a Bloomberg screen that does not constitute issuer information under Rule 433 would not be covered by the issuer's representations or warranties or indemnity or by outside counsels' negative assurance letters.

Use of Bloomberg Screens to Achieve Conveyance for Rule 159 Purposes

Thus far, we have discussed Bloomberg screens as they have been used historically—to announce the launch of a fixed income offering along with disclosure of preliminary terms, and to confirm final terms of a completed offering. Because of the wide use of Bloomberg terminals by institutional investors, Bloomberg screens also present a means by which to convey material information to such investors prior to the time of contract of sale for purposes of Rule 159 under the Securities Act.[23] Since the effective date of the offering reforms, Bloomberg screens have been used as a conveyance tool in some equity offerings as well as in fixed income offerings.[24] The ability to attach other documents to certain forms of Bloomberg communications can also be relevant in these situations.

Bloomberg screens are not effective as the sole means of conveyance in offerings involving retail investors, since it is unlikely that the retail

investors will be subscribers to the Bloomberg system. Bloomberg screens can, however, serve as an effective component of an overall conveyance strategy in virtually any offering. For example, depending on the facts and circumstances of a particular offering, a Bloomberg screen that is filed as both a free writing prospectus and as a Current Report on Form 8-K could achieve conveyance to both the institutional and retail investors if the deal permitted sufficient time for the information conveyed by the 8-K to be absorbed by the market.[25] The time needed to achieve conveyance in this manner may be greater than in an institutional-only offering, particularly if there are a larger number of retail investors. Alternatively, if there are a small number of retail investors in an offering, a Bloomberg screen that is filed as a free writing prospectus could achieve conveyance to institutional investors, while the new information could be conveyed orally to each retail investor by salespeople at the underwriting firms involved in the offering. The precise means by which to most effectively achieve conveyance in a particular situation will, of course, be dependent on the facts and circumstances present at the time.[26]

NOTES

1. References herein to fixed income transactions include offerings of both straight debt and equity-linked securities. The analysis herein does not address the use of term sheets and similar communications in offerings of asset-backed and similar securities.

2. Securities Offering Reform, Release No. 33-8591 (July 19, 2005) [70 FR 44722], as supplemented by the technical amendments effected by Release No. 33-8591A (Feb. 6, 2006) [71 FR 7411] (collectively, the Offering Reform Adopting Release). The offering reforms were proposed in Release No. 33-8501 (Nov. 3, 2004) [69 FR 67392] (the Offering Reform Proposing Release and, collectively with the Offering Reform Adopting Release, the Offering Reform Releases).

3. This functionality would be equally available in any other real-time email system that is widely used by the investing community.

4. Prior to the adoption of the offering reforms, the confirmation would be accompanied or preceded by a final prospectus. Since the December 1, 2005, effective date of the offering reforms, for most offerings the final prospectus that is filed within the required time period mandated by Rule 424 under the Securities Act will be deemed to accompany or precede the security on an "access equals delivery" basis pursuant to new Rule 172(b) under the Securities Act.

5. Rule 134 is available to all issuers other than investment companies and business development companies.

6. Offering Reform Adopting Release at p.85; Offering Reform Proposing Release at p.63. It is possible to rely on Rule 134 to disclose a portion of the terms of a security, with the balance conveyed orally or by other means.

7. To the extent that Bloomberg screens are used as term sheets, the offering reforms permit broader use of this tool than is generally the case for other free writing prospectuses. An issuer that is an "ineligible issuer" as defined in Rule 405 is generally precluded from issuing free writing prospectuses. Such an issuer may, however, issue free writing prospectuses that contain only descriptions of the terms of the securities in the offering or of the offering itself. Rule 164(e)(2). This accommodation is not available for any ineligible issuer that, during the preceding three years, was a blank check company, a shell company or a penny stock issuer.

8. Rule 433(d)(5)(ii). Note that a final term sheet free writing prospectus must be filed with the SEC within two *calendar* days, not business days, of the later of pricing and first use. Note also that this period is measured from the time that final terms are established for all classes of the offering. In the event of a multi-tranche offering of securities that prices on different days, a final term sheet describing the first-priced tranche need not be filed until the second calendar day after the pricing of the last tranche of the offering. If there is an immaterial or unintentional failure to file or delay in filing a free writing prospectus that is required to be filed under Rule 433, Rule 164(b) provides a cure provision if specified conditions are met. Finally, the requirement to file a final term sheet free writing prospectus with the SEC under Rule 433 will not be satisfied by the filing of a prospectus supplement under Rule 424. Offering Reform Adopting Release at fn. 269.

9. Immaterial or unintentional failures to include this legend can be cured pursuant to Rule 164(c).

10. Rule 433(d)(5)(i).

11. Rule 433(g). Immaterial or unintentional failures to retain free writing prospectuses can be cured pursuant to Rule 164(d).

12. Issuer information is defined as "material information about the issuer or its securities that has been provided by or on behalf of the issuer." Rule 433(h)(2). A description of the final terms of a security or of the offering of that security is issuer information. Offering Reform Adopting Release at fn. 266 and text following fn. 279.

13. Rule 433(d)(1)(ii).

14. This pre-review approach is complicated by the fact that, as noted, in offerings involving more than one underwriter each firm tends to produce its own version of the Bloomberg final term sheet screen. To the extent that an issuer seeks to pre-review all screens in a syndicated offering, delay is far more likely to ensue.

15. Rule 433(c)(1).

16. Rule 433(c)(2)(i).

17. Offering Reform Adopting Release at pp.111–112; Offering Reform Proposing Release at pp. 98–99.

18. Note that no explicit cure provision is available should a free writing prospectus contain an impermissible legend or disclaimer. *See supra* n.10.

19. Rule 433(g). This requirement is in addition to requirements imposed by Rule 17a-4 of the Exchange Act that require broker/dealers to retain all correspondence with clients, including email correspondence. *See* Note to paragraph (g) of Rule 433.

20. *See* "The Impact of Securities Offering Reform on Underwriting Arrangements," *INSIGHTS* Vol. 19, No. 10 (October 2005).

21. Mandating issuer pre-approval of all free writing prospectuses may also raise entanglement or adoption issues such that communications that would otherwise not constitute issuer free writing prospectuses and thus not be required to be filed with the SEC by the issuer may cease to be entitled to that treatment. *See* Securities Offering Reform Questions and Answers issued by the Staff of the Division of Corporation Finance of the SEC on November 30, 2005, Question 9, which can be accessed at *http://www.sec.gov/divisions/corpfin/faqs/securities_offering_reform_qa.pdf*.

22. This memorandum can be accessed at *http://www.sia.com/key_issues/pdf/SIAUAProvisions.pdf*.

23. The functionality described in this section would be equally available in any other real-time email system that is widely used by the investing community.

24. Any such a screen would be a free writing prospectus, required to be filed by the issuer no later than the date of first use (assuming that the information contained therein constitutes issuer information). Rule 433(d)(1)(i). It is important to note that including disclosure in a free writing prospectus, whether or not filed with the SEC, does not serve to include the new information in the underlying registration statement for Section 11 purposes, and free writing prospectuses are not subject to incorporation by reference into a registration statement or prospectus.

25. A speedier alternative to 8-K conveyance to retail investors is oral conveyance.

26. While institutional investors are accustomed to receiving Bloomberg screens that are brief and limited to the launch/pricing structures described above, this need not act as a disincentive to broader use of these screens if it becomes necessary to convey additional information prior to pricing.

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