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U.S. Regulation of Public Securities Offerings & Development of Standards for Internet Offerings

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U.S. REGULATION OF PUBLIC SECURITIES OFFERINGS & DEVELOPMENT OF STANDARDS FOR INTERNET OFFERINGS

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I. INTRODUCTION

The growth of the Internet as a business medium has ignited change in the structure of the capital markets and securities industry. Issuers of securities offerings are increasingly using the Internet, electronic mail, and other electronic communication forms to conduct business with investors. Rapid exposure to a myriad of parties presents greater opportunities for investors to analyze opportunities and directly invest, but also presents dangers regarding the quality and timing of decision-making information. Given these tremendous changes to the infrastructure, how would a domestic company offer registered public securities over the Internet?

This Article begins by examining the regulatory background of registered public securities offerings in the United States. It then discusses Internet-specific rules during an offering, including: (i) issuer communications, (ii) web site content, (iii) the preliminary prospectus and tombstone ads, (iv) testing the market, (v) the electronic delivery of information, (vi) the web site publication of prospectuses, and (vii) jurisdictional challenges. It concludes by examining the Aircraft Carrier Release, a pending reform proposed in 1998.

II. REGISTERED PUBLIC OFFERINGS

A. *Disclosure*

In response to fraudulent securities behavior that contributed to poor economic conditions and ultimately the Wall Street crash of 1929, Congress promulgated the Securities Act of 1933,[1] also known as the "Truth in Securities" Act.[2] The Act's main purpose is to ensure an adequate amount of disclosure about publicly offered securities.[3]

The U.S. Securities and Exchange Commission (SEC) achieves this goal by requiring issuers to register securities with the SEC by filing a registration statement pursuant to section 5 and in accordance with the prescribed information in section 7 of the Act.[4] A registration statement consists of a prospectus, which is a document that must be distributed to potential and actual investors, as well as additional information required for public release.[5] Registration under the 1933 Act only covers "securities specified therein as proposed to be offered."[6] Unlike the Securities Exchange Act of 1934,[7] which covers an entire class of securities,[8] the 1933 Act's narrow focus means that securities registered for a public offering under it may have to be registered again for subsequent transactions. This high disclosure threshold provides full and fair disclosure which benefits investors, and offers recourse through civil remedies for violations of the Act's registration and prospectus delivery requirements or for false or misleading disclosures.[9]

Despite these benefits, the SEC's disclosure requirements have historically placed an arguably excessive burden on issuers. Originally, there were two distinct disclosure systems, one applicable to the 1933 Act and the other to the 1934 Act. In 1982, the SEC instituted an integrated system to simplify and streamline disclosure requirements.[10] The disclosure

1. 15 U.S.C.S. § 77a (2002). Please refer to http://www. law.uc.edu//CCL/sldtoc.html for the complete text of the Securities Act of 1933, the Securities Exchange Act of 1934, and related rules and regulations.

2. 1 THOMAS L. HAZEN, TREATISE ON THE LAW OF SECURITIES REGULATION 7 (1990).

3. DAVID L. RATNER, SECURITIES REGULATION 33 (6th ed. 1998).

4. An exception to this rule is made for exempted transactions under sections 3 and 4 of the Securities Act of 1933, which are beyond the scope of this Article.

5. 15 U.S.C.S. § 77f(d) (2002).

6. 15 U.S.C.S. § 77f(a) (2002).

7. 15 U.S.C.S. § 78a (2002).

8. RATNER, *supra* note 3.

9. *See* 15 U.S.C.S. §§ 77k, 77(l) (2002).

10. Adoption of Integrated Disclosure System, Securities Act Release No. 336,383, 17 C.F.R. §§ 200, 201, 229, 230, 239, 240, 249, 250, 260, 274 (Mar. 16, 1982).

requirements of the 1933 and 1934 Acts were combined to form Regulation S-K, and a form was adopted for each of three registration statement categories.[11] Form S-1 is the traditional form that requires complete issuer and transaction information in the prospectus.[12] Form S-2 requires less disclosure, and may be used by issuers who have reported for three or more years under the 1933 Act.[13] Form S-3 requires the least amount of disclosure, and may be used by issuers that meet certain requirements.[14] The SEC also allows public companies to use Form S-3 to register debt that has an investment-grade rating.[15] The differences in the three Forms mainly concern

> (1) when . . . information must be present in full in the prospectus, (2) when . . . information may be presented on a streamlined basis and supplemented by documents incorporated by reference, and (3) when . . . information may be incorporated by reference from documents in the Exchange Act continuous reporting system without delivery to investors.[16]

Form S-1 requires several disclosures from the issuer, including summary information, a description of risk factors, information regarding the use of the proceeds, and a discussion of the distribution plan of the issuer.[17] Required issuer information includes a business description, a description of property, information regarding legal proceedings, information regarding the market price of and dividends on the issuer's common equity, financial statements, and management's analysis of current operations.[18]

11. 17 C.F.R. § 229.10 (2002).

12. THOMAS LEE HAZEN, THE LAW OF SECURITIES REGULATION § 3.3 (2d ed. 1990).

13. *Id.*

14. *Id.*

15. Francis A. Bottini, Jr., *An Examination of the Current Status of Rating Agencies and Proposals for Limited Oversight of Such Agencies*, 30 SAN DIEGO L. REV. 579, 582 (1993).

16. RICHARD W. JENNINGS ET AL., SECURITIES REGULATION: CASES AND MATERIALS 184 (8th ed. 1998).

17. 17 C.F.R. § 239.11 (2002).

18. *Id.* Under Item 303 of Regulation S-K, the SEC requires issuers in a "management's discussion and analysis" (MD & A) to discuss liquidity, capital resources and results of operations and such other information necessary to an understanding of financial condition, changes in financial condition and results of operations. 17 C.F.R. § 229.303(a) (2002). The MD & A is intended to give investors short- and long-term analyses of the business including the potential effects of any uncertainties. JENNINGS ET AL., *supra* note 16, at 211. And to ensure investor understanding, Rule 421 of the 1933 Act requires that it be in plain English. 17 C.F.R. § 230.421(d)(1) (2002).

The SEC's disclosure requirements for foreign issuers seeking to make public offerings in the United States are substantially similar to those required of domestic issuers, using Forms F-1, F-2, and F-3.[19] Form F-1 is the long-form registration statement filed by foreign issuers, who are either not subject to the periodic reporting requirements of the 1934 Act, or not eligible to use Forms F-2 or F-3.[20] Forms F-2 and F-3 are short-form registration statements available after the foreign issuer has been a reporting company for a minimum of thirty-six months.[21]

Recognizing the disproportionate burden that small business issuers bore in the registration process, the SEC promulgated Regulation S-B to provide an alternative form Regulation S-K for these issuers.[22] The SEC tailored Regulation S-B to match the capabilities of small businesses.[23] A "small business issuer," defined in Rule 12b-2, is one that "(1) has revenues of less than $25,000,000; (2) is a U.S. or Canadian issuer;[24] (3) is not an investment company; and (4) if a majority owned subsidiary, the parent corporation is also a small business issuer."[25] Regulation S-B allows qualifying businesses to use Form SB-1 to sell up to $10 million of securities in any 12-month period and to use Form SB-2 for larger offerings.[26] Forms SB-1 and SB-2 are much simpler than Form S-1. Also, Regulation S-X, which governs the financial statements included in any other report filed with the SEC, is waived for small businesses.[27]

B. *The Registration Process*

Registration statements are filed on-line on the SEC's Electronic Data Gathering, Analysis, and Retrieval system (EDGAR), a publicly accessible

19. Christopher J. Mailander, *Searching for Liquidity: United States Exit Strategies For International Private Equity Investment*, 13 AM. U. INT'L L. REV. 71, 87-88 (1997).

20. *Id.*

21. *Id.* at 88.

22. 17 C.F.R. §§ 228.10, 228.101-228.103, 228.201-228.203, 228.303-228.307, 228.310, 228.401-228.405, 228.501-228.512, 228.601-228.601T, 228.701-228.702 (2002).

23. *Id.*

24. *See* Multijurisdictional Disclosure And Modifications To The Current Registration And Reporting System For Canadian Issuers, Release Nos. 33-6902; 34-29354; 39-2267 (June 21, 1991), 1991 Sec Lexis 1217. The United States has implemented the Multijurisdictional Disclosure System with Canada, which permits a single registration for cross-border offerings, *id.* *See also* Henrique de Azevedo Ferreira Franca, *Legal Aspects of Internet Securities Transactions*, 5 B.U. J. SCI. & TECH. L. 4, 29 (1999).

25. 17 C.F.R. § 240.12b-2 (2001).

26. JENNINGS ET AL., *supra* note 16, at 186.

27. *Id.*

electronic database designed to accommodate all public SEC filings.[28] Under section 8(a) of the 1933 Act, the registration statement automatically becomes effective on the twentieth day after filing.[29] The issuer can then sell the registered securities. The SEC, however, can issue a refusal order or a stop order to prevent the statement from becoming effective if it requires amendment. A refusal order is issued if a registration statement is facially incomplete or inaccurate in any material respect.[30] A stop order is issued if a registration includes an apparently untrue statement or omits a required material fact.[31] However, the SEC's limited resources are nearly inadequate to comply with section 8(b) of the Act, which requires the SEC to act within ten days after the registration statement has been filed.[32] Thus, in reality, refusal orders are generally not issued.

Although the SEC used to review every registration statement, its limited resources and the large growth in the number of filings have made it impossible to review every statement on a timely basis. Accordingly, it now engages in selective review.[33] If the SEC chooses an issuer for review, it may informally communicate with the issuer through a comment letter, also known as a deficiency letter, to insist on additions or deletions to the information provided before allowing a registration statement to become effective.[34]

C. *Section 5 Timeframe*

1. The Pre-Filing Period

Section 5(c) of the 1933 Act makes it unlawful for any person to offer to sell or buy *any* security before a registration statement has been filed.[35] An "offer" includes any unusual publicity about the issuer's business, prospects for the industry, or anything that may contribute to public interest in the securities of an issuer and which raises a serious question about

28. EDGAR, *available at* http://www.sec.gov/edgar.shtml (last visited Dec. 24, 2001); *see also* K. Robert Bertram, *Advanced Technology Issues — The Internet, and State Securities Regulation — A Primer*, 67 PA. BAR ASS'N Q. 133, 135 (1996).

29. 15 U.S.C.S. § 77h(a) (2002).

30. 15 U.S.C.S. § 77h(b) (2002).

31. 15 U.S.C.S. § 77h(d) (2002).

32. JENNINGS ET AL., *supra* note 16, at 296. Interestingly, the SEC rarely issues stop orders either, mainly due to the SEC's administrative flexibility and the practical time contraints of the investment banking business. *Id.*

33. *Id.* at 204.

34. *Id.* at 209.

35. 15 U.S.C.S. § 77e(c) (2002).

whether the publicity is part of the selling effort.[36] In fact, the SEC has even held an offering-related press release in violation of section 5(c) because it deemed the news value of the release insufficient.[37] Specifically, Rule 135 only permits an issuer to publish a notice of a proposed offering that sets forth the issuer's name, the basic terms of the securities, the amount of the offering, the anticipated timing of the offering, a brief statement of the manner and purpose, whether the issuer is directing its offering to a particular class of purchasers, and any statements required by law.[38]

Fortunately, issuers and underwriters may still negotiate the terms of the offering during the pre-filing period because section 2(a)(3) defines "offer to sell" to exclude preliminary negotiations or agreements between issuers and underwriters or among underwriters.[39] Section 4(1) further limits the application of section 5 by completely excluding activity "by any person other than an issuer,[40] underwriter,[41] or dealer."[42] Accordingly, the average

36. Re: Publication of Information Prior to or After the Effective Date of a Registration Statement, Securities Act Release No. 333,844 (Oct. 8, 1957), 1957 WL 3605.

37. In the Matter of Carl M. Loeb, Rhoades & Co., and Dominick & Dominick, 38 S.E.C. 843, Release No. 5870, 1959 WL 5953 (Feb. 9, 1959).

38. 17 C.F.R. § 230.135 (2002). Rule 135 details additional information allowed for offerings to existing security holders, offerings to employees of the issuer or an affiliated company, exchange offers, and Rule 145(a) offers. *Id.*

39. 15 U.S.C.S. § 77b(a)(3) (2002).

40. *See* 15 U.S.C.S. § 77b(a)(4) (2002). An "issuer" is defined as

> every person who issues or proposes to issue any security; except that with respect to certificates of deposit, voting-trust certificates, or collateral-trust certificates, or with respect to certificates of interest or shares in an unincorporated investment trust not having a board of directors (or persons performing similar functions) or of the fixed, restricted management, or unit type, the term "issuer" means the person or persons performing the acts and assuming the duties of depositor or manager pursuant to the provisions of the trust or other agreement or instrument under which such securities are issued; except that in the case of an unincorporated association which provides by its articles for limited liability of any or all of its members, or in the case of a trust, committee, or other legal entity, the trustees or members thereof shall not be individually liable as issuers of any security issued by the association, trust, committee, or other legal entity; except that with respect to equipment-trust certificates or like securities, the term "issuer" means the person by whom the equipment or property is or is to be used; and except that with respect to fractional undivided interests in oil, gas, or other mineral rights, the term "issuer" means the owner of any such right or of any interest in such right . . . who creates fractional interests therein for the purpose of public offerings.

Id. See also Dennis S. Corgill, *Securities As Investments At Risk*, 67 TUL. L. REV. 861, 936 (1993).

41. *See* 15 U.S.C.S. § 77b(a)(11) (2002). An "underwriter" is defined as

investor who buys and sells for his own account is free from any of these restrictions.

2. The Waiting Period

In contrast to the situationally defined pre-filing period, there is a statutorily defined "waiting period" or "cooling-off period" that is triggered by the filing of the preliminary prospectus and continues until the registration statement becomes effective.[43] Section 5 of the Securities Act of 1933 does not restrict oral offers during the waiting period. Nevertheless, section 5(a)(1) prohibits any actual sales from occurring during this waiting period.[44] Although section 5 permits offers to sell, it restricts the use of a "prospectus," which section 2(a)(10) broadly defines as any written, radio, or television communication that offers a security for sale, to those that meet the requirements of section 10. It is difficult to meet the requirements of section 10, however, because the registration statement has not yet become effective, and thus, some of the required information is generally unavailable during the waiting period. Consequently, the SEC allows the use of a preliminary prospectus, a tombstone ad,[45] and testing of the market during this time.[46]

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any person who has purchased from an issuer with a view to, or offers or sells for an issuer in connection with, the distribution of any security, or participates or has a direct or indirect participation in any such undertaking, or participates or has a participation in the direct or indirect underwriting of any such undertaking; but such term shall not include a person whose interest is limited to a commission from an underwriter or dealer not in excess of the usual and customary distributors' or sellers' commission. As used in this paragraph the term "issuer" shall include, in addition to an issuer, any person directly or indirectly controlling or controlled by the issuer, or any person under direct or indirect common control with the issuer.

Id. See also Therese Maynard, *The Future of Securities Act Section 12(2)*, 45 ALA. L. REV. 817, 850-65 (1994).

42. *See* 15 U.S.C.S. § 77b(a)(12) (2002). A "dealer" is defined as "any person who engages either for all or part of his time, directly or indirectly, as agent, broker, or principal, in the business of offering, buying, selling, or otherwise dealing or trading in securities issued by another person," *id. See also* Samuel N. Allen, *A Lawyer's Guide to the Operation of Underwriting Syndicates*, 26 NEW ENG. L. REV. 319, 322 (1991).

43. *See* 15 U.S.C.S. §77e (2002).

44. 15 U.S.C.S. § 77e (2002).

45. Memorandum of the Statutory Revision Committee, Securities Act Release No. 333,224 (June 6, 1947), 1947 WL 6715 [hereinafter Statutory Revision Memo].

46. 17 C.F.R. § 230.134(d) (2002).

a. The Preliminary Prospectus

During the waiting period, section 10(b) of the Securities Act of 1933 authorizes issuers to publish a preliminary prospectus which omits the unavailable information that is required by section 10(a).[47] Specifically, the SEC promulgated Rule 430, which provides that the preliminary prospectus may omit information about the offering price, discounts or commissions given to the underwriters or dealers, proceeds, conversion rates, call prices, or other matters dependent upon the offering price.[48] Regulation S-K, Item 501(10), requires the preliminary prospectus to contain a prominent caption entitled "Subject to Completion" and a legend which explains that the prospectus is not an offer to sell the securities.[49] Moreover, Rule 15c2-8 of the 1934 Act requires brokers and dealers to send preliminary prospectuses to all potential buyers at least forty-eight hours before the sales confirmations are sent, and to take reasonable steps to make copies of the preliminary prospectus available to securities sales representatives and to any person who makes a written request for one.[50] This preliminary prospectus is, as its name denotes, preliminary in nature; a final prospectus replaces the preliminary prospectus once the registration statement becomes effective.

b. The Tombstone Ad

The "tombstone ad" is written communication which ascertains prospective buyers' level of interest before delivering a statutory prospectus.[51] According to Rule 134, a tombstone ad does *not* fall within the section 2(a)(10) definition of a "prospectus" because it is published after a registration statement has been filed and contains only specified information. Such specified information includes: the name of the issuer, the title of the security, a brief indication of the general type of business of the issuer, the price of the security, any applicable debt-related interest provisions, the name and address of the sender of the communication, the names of the managing underwriters, and the approximate date for the proposed sale.[52]

47. 15 U.S.C.S. § 77j(b) (2002).
48. 17 C.F.R. § 230.430 (2002).
49. 17 C.F.R. § 229.501(10) (2002).
50. 17 C.F.R. § 240.15c2-8 (2002).
51. Statutory Revision Memo, *supra* note 45.
52. 17 C.F.R. § 230.134 (2002).

c. Testing the Market

Pursuant to Rule 134(d), the managing underwriter or broker may "test the market" during the waiting period by contacting prospective members of the selling group orally or through the preliminary prospectus in order to solicit indications of interest or offers to buy.[53] Testing the market is a useful, cost-effective means of assessing whether there is sufficient interest in the investment to proceed with an offering. The underwriter or broker may also prepare a "book," listing expected buyers for the securities, and stage "roadshows" in which meetings are held with different financial professionals at various locations to gage interest in an offering and set pricing.[54]

(1) Solicitation of Interest and Offers

Soliciting indications of interest allows the issuer to focus its securities marketing efforts.[55] Issuers or underwriters can gather information on market reception to a certain price level by making sales offers to investors. An investor's indication of interest entails no obligation or commitment by the investor. In fact, Rule 134(d) requires offers to state that acceptance cannot occur until the registration statement becomes effective and that offers may be revoked at any time prior to an acceptance given after the registration statement's effective date.[56]

(2) Roadshows

Roadshows are central to the marketing process. A roadshow is usually a series of national and international meetings at which senior management present corporate financial projections. Attendance is usually limited to securities firms and institutional investors, excluding the press and the general public.[57] Written materials other than the preliminary prospectus are not to be used in the roadshow.[58] However, in actuality, written materials are typically distributed during the presentation and collected at the conclusion of the meeting. In addition to allowing interest assessment, roadshows permit a dialogue between investors and issuers.[59]

53. 17 C.F.R. § 230.134(d) (2002).

54. JENNINGS ET AL., *supra* note 16, at 143.

55. Wit Capital Corp., 1999 SEC No-Action Letter, LEXIS 620, at *47.

56. 17 C.F.R. § 230.134(d) (2002).

57. JENNINGS ET AL., *supra* note 16, at 145.

58. 15 U.S.C.S. § 77e (2002).

59. *See generally* Mark Leibovich, *Journey Into the Secret Heart of Capitalism: Cross-Country "Roadshow" Marks a Young CEO's Stock Market Debut*, WASH. POST, Aug. 9, 1998, at A1.

3. The Post-Effective Period

After the registration statement becomes effective, underwriters and dealers may accept waiting-period offers to buy and may sell the new securities to anyone, but section 5(b)(2) requires that the securities be accompanied or preceded by a prospectus.[60] Section 4(1) exempts from section 5 provisions any *person* other than issuers, underwriters, or dealers, *supra*. In addition, section 4(3) exempts all *sales* by dealers, except for two classes of sales:

> (1) the original sale by the dealer of the securities which are [sic] being distributed by the issuer or by or through an underwriter, no matter how long the dealer has held them (§ 4(3)(C)); and
>
> (2) resales by the dealer of securities which were sold to the public in such a distribution and reacquired by the dealer, but only if they take place within a specified period after the original public offering (§ 4(3)(A) and (B)).[61]

Rule 174 simplifies the section 5(b)(2) requirement by providing that a dealer does not need to deliver a prospectus on a resale of a security if the issuer was subject to the reporting requirements of the 1934 Act immediately prior to filing the registration statement.[62]

D. *Blue Sky Laws*

Whenever an issuer conducts a securities offering, the issuer must consider relevant state law. All states have laws regulating securities transactions within their borders. These regulations are known as "blue sky" laws.[63] In an attempt to move towards uniformity, the Commissioners on Uniform State Laws promulgated the Uniform Securities Act (Uniform Act) in 1956.[64] The Uniform Act is divided into four parts: (1) anti-fraud provisions; (2) broker-dealer registration; (3) security registration; and (4) definitions, exemptions, and administrative and liability provisions.[65] Approximately thirty states have adopted some of the provisions of the Uniform Act, and most of them made substantial textual changes and

60. 15 U.S.C.S. § 77e(b)(2) (2002).

61. RATNER, *supra* note 3, at 51.

62. 17 C.F.R. § 230.174 (2002).

63. Hall v. Geiger-Jones, 242 U.S. 539, 550 (1917). These regulations get their name from a 1917 judicial opinion describing them as preventing "speculative schemes which have no more basis than so many feet of blue sky." *Id.*

64. RATNER, *supra* note 3, at 300.

65. *Id.* at 300-01.

interpret the language differently.[66] Major commercial states, including Texas, California, New York, and Illinois, have not adopted any part of the Uniform Act.[67] Still, the promulgation of the Uniform Act has accomplished a greater degree of consistency than had previously existed.[68]

Traditionally, issuers of public offerings had to comply with the blue sky laws of each state in which they offered securities, despite the fact that most state blue sky laws do not explicitly define when an offer is made in its state.[69] Due to this ambiguity, issuers of large offerings often have difficulty determining when and where they have blue sky obligations, and encounter conflict of law issues in civil actions where the buyers and sellers reside in separate states.[70] To simplify this onerous process of complying with the various potentially conflicting laws, Congress enacted the National Securities Market Improvement Act (NSMIA) in 1996.[71] Through NSMIA, the SEC preempts blue sky laws for certain securities, such as those listed on an exchange, issued by a registered investment company, sold to qualified purchasers, and certain exempt securities under the 1933 Act.[72] Although NSMIA preempts significant areas of blue sky laws for registered public corporations, it does not simplify the registration process for publicly offered securities subject to certain federal registration exemptions.[73] Specifically, NSMIA leaves (1) small issues offered pursuant to Rule 504; (2) limited offerings issued pursuant to Rule 505; (3) intrastate offerings pursuant to section 3(a)(11) or Rule 147; and (4) securities offered pursuant to Regulation A under the regulatory control of the individual states.[74] Thus, blue sky laws remain an obstacle for companies seeking to conduct public offerings on the Internet in any of the categories exempted from NSMIA.

III. REGULATORY ADAPTATIONS TO AN ELECTRONIC REGIME

Technological innovation and creativity have contributed enormously to efficient capital allocations and the liquidity of shareholder investments. Electronic communications are now nearly ubiquitous and thus indispensable for efficient transactions. Unavoidably, new ways of

66. *Id.* at 301.
67. *Id.*
68. *Id.*
69. RATNER, *supra* note 3, at 310-11.
70. *Id.*
71. *Id.*
72. 15 U.S.C.S. § 77r(b)(1) (2002).
73. *Id.*
74. Kevin A. Jones, Note, *The National Securities Markets Improvement Act of 1996: A New Model For Efficient Capital Formation*, 53 ARK. L. REV. 153, 170 (2000).

communicating present new problems. E-mail blurs the distinction between oral and written communication, sometimes acting as an oral communication because it facilitates an interactive and expedient dialogue. But e-mail sometimes also acts as written communication, for example, when it is used in lieu of postal mail for sending documents. In a 1996 release, the SEC indicated that the legal status of e-mail was not fixed, and depends on whether it is substituted for telephone conversations.[75] The status of interactive discussions in on-line forums, bulletin boards, message centers, and chat rooms, and whether there should be a set of practices for issuers that host on-line discussion forums, is yet unresolved.[76]

A. *Activities & Disclosure Generally*

1. Issuer Communications During an Offering

Beyond the oral-written distinction, the SEC stated in 2000 that "an issuer in registration must consider the application of Section 5 of the Securities Act to all of its communications with the public . . . includ[ing] information on an issuer's website as well as information on a third-party website to which the issuer has established a hyperlink."[77] The SEC has indicated that an issuer in registration should limit such communications to ordinary business and financial information, which may include the following:

> advertisements concerning the issuer's products and services;
> Exchange Act reports required to be filed with the Commission;
> proxy statements, annual reports to security holders and dividend notices;
> press announcements concerning business and financial developments;
> answers to unsolicited telephone inquiries concerning business matters from securities analysts, financial analysts, security holders and participants in the communications field who have a legitimate interest in the issuer's affairs; and

75. Use of Electronic Media by Broker-Dealers, Transfer Agents and Investment Advisors for Delivery of Information, Securities Act Release No. 337,288, 17 C.F.R. §§ 231, 241, 271, 276 (May 9, 1996).

76. Use of Electronic Media, SEC Interpretative Release No. 3,442,728 at ¶ D7 (Apr. 28, 2000), *available at* http://www.sec.gov/rules/interp/34-42728.htm (last visited Dec. 17, 2002).

77. *Id.* ¶ B2.

security holders' meetings and responses to security holder inquiries relating to these matters.[78]

Communication or information in these areas may be posted on an issuer's web site or associated with it through hyperlinks.[79] The SEC's cautionary statements mean that there must be heightened review of an issuer's web site and constant monitoring of any hyperlinked information to ensure compliance with section 5.

2. Web Site Content During an Offering

a. The "Envelope Theory"

The "envelope theory" is the concept that documents in close proximity on the same web site or hyperlinked to each other are treated as though delivered to the user in the same paper envelope.[80] This is important because sales literature in a registered public offering cannot be delivered until the registration statement is effective and a final prospectus accompanies or precedes the sales literature.[81] Accordingly, an issuer must be particularly careful during registration that its web site content contains only materials or free writing the issuer intends to be part of the prospectus.

The SEC has indicated that a document that is hyperlinked to a section 10 prospectus is not considered part of the prospectus, but is considered to be delivered with the prospectus.[82] This position is ambigious and a substantial cause for concern with respect to issuer liability. In fact, it seems to state the untenable position that an issuer is liable for literature hyperlinked to its section 10 prospectus from anywhere on the Internet, even though the existence and content of such a link may change continuously and may be created and managed by independent parties unknown to, and beyond the control of, the issuer.

The SEC's position on free writing is even less clear. The SEC has only indicated that web site content must be reviewed to determine whether it contains impermissible free writing.[83] Temporally, it is not clear whether the SEC is advocating active monitoring of all of an issuer's web site hyperlinks. If so, the SEC is unclear on how often or according to what

78. *See id.*

79. *See id.*

80. *Id.* ¶ A4.

81. Use of Electronic Media, *supra* note 76, at ¶ A4.

82. *Id.*; *see* Part II.B. *The Registration Process infra* for further discussion of hyperlinked material.

83. *See* Use of Electronic Media, *supra* note 76, ¶ A4.

parameters this should be done. It is also interesting to posit whether a disclaimer may relieve an issuer of such liability.

b. Issuer Responsibility

Issuers and other financial intermediaries are responsible for the accuracy of their statements, regardless of the medium through which the statements are made.[84] The issuer's involvement in the preparation of the information, explicit or implicit endorsement of the information, context of the hyperlink, risk of confusion and presentation of the hyperlinked information are factors that the SEC will consider in making a liability assessment.[85]

B. *The Registration Process*

During the registration process, the SEC has indicated that web site content is considered part of a section 10 prospectus only if the issuer acts to make it part of the prospectus, for example, by including a hyperlink within a section 10 prospectus.[86] In this case, the hyperlinked information would be included in the prospectus, and would have to be filed as part of the prospectus in the registration statement.[87]

C. *Section 5 Timeframe*

1. The Pre-Filing Period

There are no changes specific to electronic offerings for the period prior to the filing of the registration statement.

2. The Waiting Period

a. The Preliminary Prospectus

Similar to the hyperlinks in the final prospectus, the SEC has made it clear that hyperlinks embedded within the preliminary prospectus do not implicate federal securities law, but do become part of the prospectus and must be filed with the SEC.[88] Additionally, written consent must be obtained from the author of any hyperlinked document and filed with the

84. *Id.* ¶ B1.
85. *Id.* ¶ B1(a)-(c).
86. *See id.* ¶ A4.
87. *Id.*
88. Use of Electronic Media, *supra* note 76, exs.6-7.

SEC. The hyperlinked document will then be subject to section 11 liability and the anti-fraud provisions of the federal securities laws.[89]

b. The Tombstone Ad

The SEC has clearly indicated that an issuer may post a tombstone ad on its Internet web site, provided the tombstone ad complies with Rule 134.[90] Additionally, the issuer may include its Internet address in the tombstone ad so that potential investors may obtain an electronic prospectus.[91]

c. Testing the Market

(1) Solicitation of Interest and Offers

Although the language of Rule 134(d) is silent on the issue, the SEC has recognized electronic communication of solicitations of interest and offers to buy.[92] This is important because it enhances issuer and investor flexibility and expedites purchasing new issues. In a 1996 no-action letter to IPONET, the SEC confirmed that Rule 134(d) permits investors to submit indications of interest through electronic coupons or cards.[93]

In 1999, the SEC confirmed in a no-action letter to Wit Capital that Rule 134(d) also permits electronic conditional offers to buy.[94] The SEC established that Wit Capital can confirm an investor's conditional offer via e-mail two days prior to the effective date of the offering, and that an investor can convert his indication of interest into a firm offer by responding to Wit Capital's confirmation e-mail.[95] After the registration statement becomes effective and the offering is priced, Wit Capital can accept the investor's conditional offer.[96]

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89. *Id.* ex. 6.

90. Use of Electronic Media for Delivery Purposes, Securities Act Release No. 337,233, ex. 18 (Oct. 13, 1995), *available at* http://www.sec.gov/rules/interp/33-7233.txt (last visited Dec. 17, 2002).

91. *Id.* ex. 19.

92. IPONET, 1996 SEC No-Action Letter, LEXIS 642, at *1.

93. *Id. Cf.* Lamp Technologies, Inc., 1998 SEC No-Action Letter, LEXIS 615 (discussing web site solicitation of interest and offers in private placements under Regulation D of the 1933 Act). Under IPONET's system, investors can hyperlink to an electronic coupon embedded in IPONET's on-line prospectus to indicate their interest in the issue, e-mail their broker directly, or print the coupon and send it by postal mail. IPONET, SEC No-Action Letter at *8.

94. Wit Capital Corp., *supra* note 55, at *1-*2.

95. *Id.*

96. *Id.*

(2) Internet Roadshows

The advent of Internet roadshows is a significant advancement in the securities field because of their tremendous advantages over physical roadshows. Virtual roadshows level the playing field for securities firms and institutional investors who are otherwise unable to attend.[97] They have the potential to enhance the quality of information because the participants in the roadshow know that a broader audience is capable of viewing their presentations (including the SEC).[98] Moreover, Internet roadshows give investors more time to consider their investments because the preliminary prospectus must be delivered earlier in order to comply with the SEC's requirement that an investor view the preliminary prospectus prior to, or at the same time as, the roadshow.[99]

Despite these advantages, issuers have shunned virtual roadshows until recently out of fear that the electronic nature of the transmission would transform the roadshow from an oral to a prohibited written presentation, thus falling within the definition of a prospectus in section 2(a)(10) and becoming subject to section 5(b)(1).[100] The cause for concern stemmed from the language of section 2(a)(10), which defines "prospectus" to include "any . . . communication, written or by radio or television, which offers a security for sale."[101] As section 5(b)(1) prohibits the use of any prospectus other than that which meets the requirements of section 10 during the waiting period, this would essentially defeat the central marketing feature of the roadshow.

However, the SEC has made it clear that prohibited information is not transmitted by a virtual roadshow. In a 1997 no-action letter, the SEC permitted the Private Financial Network (PFN), a subsidiary of an MSNBC joint venture between NBC and Microsoft,[102] to broadcast issuer roadshows, either on a live or delayed basis, to its subscribers over its private network under the assumption that such communications would not fall within the definition of a prospectus under section 2(a)(10).[103] The rationale was that a prospectus under section 2(a)(10) was "intended to

97. Net Roadshow, Inc., SEC No-Action Letter, [1997 Transfer Binder] Fed. Sec. L. Rep. (CCH) P 77,367, at 77,849, LEXIS 864, at *10 (Sept. 8, 1997).

98. *Id.*

99. *Id.*

100. Linda C. Quinn & Ottilie L. Jarmel, *The Road Less Traveled: The Advent of Electronic Roadshows*, INSIGHTS, July 1997, at 3, *construed in* Jonas A. Marson, Comment, *Surfing the Web for Capital: The Regulation of Internet Securities Offerings*, 16 COMPUTER & HIGH TECH. L.J. 281, 295 (2000).

101. 15 U.S.C.S. § 77b(a)(10) (2002).

102. Marson, *supra* note 100, at 295 n.89.

103. *Id.* at 296.

reach to those documents or communications that are widely disseminated to an undifferentiated public" as opposed to select invited members.[104]

Later in 1997, the SEC authorized Net Roadshow[105] to transmit roadshows directly over the Internet,[106] and in 1999 the SEC expanded the audience to include accredited investors[107] instead of limiting access solely to institutional investors.[108] Accredited investors were then free to contact one of the underwriters of an issue in order to obtain an access code and then view the roadshow directly from Net Roadshow's web site.[109] Currently, sophisticated investors and financial institutions are privy to financial projections and other valuable information to the disadvantage of the average investor. This disparity in information distribution is unnecessary and anachronistic in the Internet era. The SEC seems to realize this: The Aircraft Carrier Release, *infra* Section IVa, would make virtual roadshows available on-line to all investors without restriction.[110]

3. The Post-Effective Period

a. Electronic Delivery

Internet-related issues in the post-effective period focus exclusively on investors' receptiveness to electronic delivery through a specified electronic medium, awareness that electronic delivery has occurred, and access to information. Generally, the SEC believes that electronic delivery satisfies federal securities law delivery requirements "if such distribution results in the delivery to the intended recipients of substantially equivalent information as these recipients would have had if the information were delivered to them in paper form."[111] As with physical paper delivery, the SEC requires that there is an opportunity to retain a permanent record of the information.[112]

104. Private Financial Network, 1997 SEC No-Action Letter, LEXIS 406 at *13.

105. Net Roadshow, Inc., *supra* note 97.

106. *Id.* at *1.

107. *See* 17 C.F.R. § 230.501(a) (2002).

108. Allyson Vaughan, *Firm Gets Approval From SEC to Include Individuals in Virtual Roadshows*, 25 CORP. FINANCING WK. 6, Feb. 8, 1999, at 1, *construed in* Lisa A. Mondschein, Note, *The Solicitation and Marketing of Securities Offerings Through the Internet*, 65 BROOK. L. REV. 185, *213 (1999).

109. Net Roadshow, Inc., *supra* note 97, at *5-*6.

110. The Regulation of Securities Offerings, Securities Act Release No. 337,606A, 63 Fed. Reg. 67,174 (Nov. 13, 1998), *available at* http://www.sec.gov/rules/proposed.shtml (last visited Dec. 13, 2002).

111. Use of Electronic Media for Delivery Purposes, *supra* note 90, at 7.

112. *Id.*

(1) Consent

Consent is the most critical issue with the electronic delivery of disclosure documents. The SEC permits issuers to obtain consent via the telephone, electronic communication, or written communication, as long as the consent is "informed."[113] Consent is considered "informed" if the financial intermediary: (1) specifies the manner of delivery to which the investor is consenting (i.e., e-mail, Internet web site); (2) advises the investor that he may incur certain costs associated with electronic delivery (i.e., on-line time, printing); (3) advises the investor of the possible risks (i.e., system outages) of electronic delivery; and (4) advises the investor that the consent is indefinite but that it can be revoked at any time.[114]

In all cases, the issuer must keep a record of the consent, indicating whether the consent is global, what electronic media will be used,[115] and ensuring the investor's authenticity.[116] The SEC has specified that an issuer can verify authenticity through either personal knowledge of the investor, or through the use of a personal identification number.[117]

The SEC has confirmed that an investor may also simultaneously consent to the electronic delivery of documents. Issuers may rely on explicit investor consent[118] provided to underwriters, brokerage firms, and other service providers, and vice versa.[119] Furthermore, investors may consent to electronic delivery of *all* documents of *any* issuer in which that investor buys or owns securities through a particular intermediary as long as the consent is informed.[120] This is referred to as "global consent." Due to the broad scope of global consent, issuers should take special care to ensure that investors understand its breadth and that the investors have the right to revoke their consent at any time.[121] Although a global consent must specify the types of electronic media that may be used, it need not identify which medium a particular issuer will use or which issuers are covered.[122]

(2) Notice

The SEC recognizes that an electronic document is analogous to a physical paper document, and has indicated that an electronic document in

113. Use of Electronic Media, *supra* note 76, ¶ A1.
114. *Id.* ¶E ex. 2.
115. *Id.* ¶A1 n.22.
116. *Id.* ¶ A1.
117. *See id.* exs. 1-2.
118. Use of Electronic Media, *supra* note 76, ¶ D3.
119. *Id.* ¶ A2.
120. *Id.*
121. *Id.*
122. *Id.*

the form of a computer disk, CD-ROM, audiotape, videotape, or e-mail will suffice as notice.[123] If disclosure documents are posted on a company web site or in an investor's account at his broker-dealer's web site, the SEC requires a separate notice to be provided to the investor,[124] unless the issuer can show that delivery has otherwise been satisfied, *infra* Section III3a(4).[125] This separate notice can be either in the form of an electronic or a physical document.

(3) Access

Even with their dramatic growth in popularity, computers and Internet access are currently neither ubiquitous nor uniform. Accordingly, the SEC insists that the investor be capable of accessing and retaining information (i.e., by downloading)[126] in a way that is not unreasonably burdensome.[127] The SEC has established that if an investor must proceed through a confusing series of ever-changing menus to access a required document so that access would generally not occur, this procedure would be "unduly burdensome," and delivery would not be deemed to have occurred unless the issuer could otherwise show.[128]

Still, the issuers must provide a paper version of the documents for use in the event of a system failure, computer incompatibility, revocation of consent by the investor, or a request for a paper copy by the investor.[129] Oddly, the SEC has stated that this requirement does not preclude an "electronic-only" offering, which is an offering in which investors may only participate if they accept electronic delivery of all documents.[130] Rather the SEC paradoxically requires that an issuer in an electronic-only offering provide the required documents in paper form if investors revoke their consent before a valid delivery has been made or whenever investors request.[131]

(4) Evidence of Delivery

The SEC recognizes that electronic delivery, like postal delivery, provides reasonable assurance that the delivery requirement has been

123. Use of Electronic Media for Delivery Purposes, *supra* note 90, at 8.
124. Use of Electronic Media, *supra* note 76, ¶ D2.
125. *See* Use of Electronic Media for Delivery Purposes, *supra* note 90, at 8.
126. *Id.* at 9 n.25.
127. *Id.* at 8-9.
128. *Id.* at 8-9 n.24.
129. *Id.* at 9.
130. *See* Use of Electronic Media for Delivery Purposes, *supra* note 90, at 9.
131. Use of Electronic Media, *supra* note 76, ¶ D4.

satisfied. To guide issuers, it has outlined five examples of procedures evidencing satisfaction of delivery requirements:

> (1) obtaining an informed consent from an investor to receive the information through a particular electronic medium coupled with assuring appropriate notice and access;
> (2) obtaining evidence that an investor actually received the information, for example, by electronic mail return-receipt or confirmation of accessing, downloading, or printing;
> (3) disseminating information through certain facsimile methods;
> (4) an investor's accessing a document with hyperlinking to a required document; and
> (5) using forms or other material available only by accessing the information.[132]

b. Web Site Publication of Prospectuses

In a 1995 release, the SEC stated that "absent other factors such as express consent from the investor or an investor's actually accessing the document on the Web site, the procedures [evidencing satisfaction of delivery requirements] by themselves would not satisfy the delivery requirements under the Securities Act."[133] The rationale here appeared to be concern that a prospectus may be posted but not received by the investor, leading to an uninformed investment decision.

In its most recent release, the SEC declined to elaborate on this issue or prescribe procedures to be followed in web site publications of prospectuses.[134] Screening access to information in connection with a securities offering by prospective customers is important so that the distributed information can be limited to that which is (i) filed with the SEC as part of the public offering and (ii) covered by Rule 134.[135] Unfortunately, the SEC has merely stated that it "will continue to analyze this area as practice, procedures and technology evolve, with a view to possible regulatory action in the future,"[136] and has referred readers to its Wit Capital no-action letter in which it simply "noted" Wit Capital's position.[137]

Although the SEC did not directly address the concern stated in the 1995 Release, Wit Capital received implicit approval for its web site methodology in which it established a separate area of its web site

132. Use of Electronic Media for Delivery Purposes, *supra* note 90, at 10-11.
133. *Id.* at 11 ex. 1.
134. Use of Electronic Media, *supra* note 76, ¶ C1.
135. Wit Capital Corp., *supra* note 55, at *21.
136. *See* Use of Electronic Media, *supra* note 76, ¶ C1.
137. Wit Capital Corp., *supra* note 55, at *2-*3.

containing a copy of the prospectus, a Rule 134 notice, and additional informational web pages for each public offering in which it participated.[138] Visitors could reach this distinct area from Wit Capital's general web site through a hyperlink to a web page that listed securities offerings in which Wit Capital was participating.[139] Strengthening this division in its web site, Wit Capital prevented visitors from hyperlinking back to the general web site from this segregated area.[140] This separated area did not provide "quotes, news or research concerning the subject securities or any other securities by direct hyperlink."[141]

At approximately the same time the paper version of the preliminary prospectus was provided to customers, Wit Capital posted a copy of that same preliminary prospectus on its web site and sent an e-mail to its members[142] in accordance with Rule 134 notifying them of the offering, notifying them of the posting of the preliminary prospectus, and containing a hyperlink to the segregated area of the Wit Capital web site containing the preliminary prospectus.[143] If a preliminary prospectus was amended, Wit Capital promptly made the amended version available on the segregated area of its web site, sent an e-mail notifying customers who had transmitted conditional offers to buy shares in the offering of the amended version, and provided a hyperlink to the amended prospectus in the e-mail.[144]

Wit Capital also limited access to certain pages within its segregated area. To achieve this access restriction, it structured its web site navigational system so that members had to first complete Wit Capital's Registration page. Members were required to enter their e-mail addresses and then brought to the Prospectus Links page before they could navigate within the segregated area to either the Pre-Conditional Offer page or the Conditional Offer page.[145] In addition, members had to open accounts and become customers before they could submit conditional offers.[146]

138. *Id.* at *10.

139. *Id.* at *20.

140. *Id.*

141. *Id.* at *21.

142. Wit Capital Corp., *supra* note 55, at *11. Wit Capital defined a "member" as a "person who has provided an e-mail address to Wit Capital." *Id.* It distinguishes members from customers, which are those who have opened accounts with Wit Capital and can therefore participate in offerings. *Id.*

143. *Id.*

144. *Id.* at *18-*19.

145. *Id.* at *12-*13.

146. *Id.* at *13-*14.

D. *Jurisdictional Challenges*

When an issuer files a registration statement on-line through EDGAR, the question arises as to whether the issuer violates a state's securities regulations by circulating a copy of a prospectus within that state before filing a registration statement for that state.[147] Sometimes called "gun jumping," this violation would make subsequent state registration difficult or impossible.[148] Moreover, it is not clear if an issuer would be in violation of state securities laws for encouraging potential offerees to obtain a copy of its prospectus from EDGAR or its company Internet web site.[149]

Arguably, when an issuer places material on the Internet, it places it within the jurisdiction of every state.[150] It is unclear if an Internet issuer can effectively shield itself from state jurisdiction with a disclaimer, or how a court would react to a state's assertion of jurisdiction over such an Internet transaction.[151] Without clear and uniform guidelines, interstate securities offerings pose uncertain consequences, and accordingly, amplified risk.

IV. PROPOSED CHANGES: THE AIRCRAFT CARRIER RELEASE

A. *Registration System Reform*

In 1998, the SEC proposed a set of significant changes to the securities regulatory framework, dubbed the "Aircraft Carrier Release" because it is an enormous project that would fundamentally change the registration and offering of securities under the 1933 Act.[152] Prompted by technological innovations that enable instant communications, the rise of the Internet, and a variety of other factors, the SEC aims to streamline the registration process and increase the timing and disclosure flexibility of registered offerings, while maintaining investor protection.[153] Since the Aircraft Carrier Release's proposal in 1998, it seems unlikely that it will be adopted in its current form. However, it provides an indication of the general direction of SEC regulation.

The Aircraft Carrier Release would provide greater control and predictability for issuers. It would replace the existing registration statement

147. Bertram, *supra* note 28, at 136.

148. *Id.*

149. *Id.*

150. *Id.*

151. *Id.*

152. SEC Commissioner Isaac C. Hunt, Jr., Address at the Practicing Law Institute's 30th Annual Institute on Securities Regulation (Nov. 5, 1998).

153. The Regulation of Securities Offerings, *supra* note 110, at *67,178.

forms with a three-tiered registration system for offerings.[154] This system would consist of three new forms: Form A for smaller or unseasoned companies; Form B for larger, seasoned, well-followed issuers and offerings made to relatively informed or sophisticated investors; and Form C for business combinations or exchange offers.[155] Larger, seasoned issuers would be able to offer securities at any time as long as they filed a registration statement before the sale of the securities.[156] Small, seasoned issuers would also be able to offer securities at any time when making offerings to "relatively sophisticated or informed investors."[157] These issuers would be able to designate the effective dates of their registration statements, and the registration statement would become effective without review on the specified date.[158]

B. *Communications During an Offering*

The Aircraft Carrier Release would allow issuers a greater level of written communication with investors during the pre-filing and waiting periods.[159] Currently, section 5(c) prohibits offers during the pre-filing period, and section 5(b)(1) prohibits written communications relating to an offering other than a section 10(b) prospectus during the waiting period.[160] The proposed revisions would allow the use of "any document (not just the traditional prospectus) at any time during an offering by a larger seasoned issuer or an offering to sophisticated or informed investors by a smaller seasoned issuer."[161] In exchange, the SEC would require the issuer to file this "free writing"[162] as part of the registration statement and be subject to the anti-fraud and civil liability provisions for statements in their free writing.[163] Similarly, all other offerings would be allowed the same flexibility after the issuer had filed a registration statement.[164] In addition,

154. *Id.* at *67,176.

155. *Id.*

156. *Id.* at *67,174.

157. *Id.* at *67,178.

158. *See* Regulation of Securities Offerings, *supra* note 110, at *67,178.

159. *Id.*

160. 15 U.S.C.S. § 77e (2002).

161. *See* The Regulation of Securities Offerings, *supra* note 110.

162. *See id.* at *67,216. The Aircraft Carrier Release indicates that free writing materials would include all written information, such as sales literature and forward-looking documents that are "disclosed by or on behalf of the issuer during the offering period." *Id.* Free writing would not include offering information (including the amount of securities being offered, disclosure of material changes to the issuer's affairs since the prior fiscal year, and disclosures pursuant to Regulation S-K), factual business communications or limited notices of proposed offerings. *Id.*

163. *See id.*

164. *Id.*

the proposed increased allowance of written communications would enable greater investor access to analyst research reports.[165]

1. Internet Roadshows

The proposed deregulation would have an uncertain impact on Internet roadshows. The proposed rules would allow issuers and market participants to "conduct electronic roadshows to institutional *and* retail investors *without* the use of password protection"[166] during the pre-filing period.[167] On the one hand, the Aircraft Carrier Release would seem to enhance issuers' ability to use virtual roadshows. By allowing free writing during the pre-filing and waiting periods, the Aircraft Carrier Release ends the need for companies to request no-action letter assurances that their practices will not violate section 5(b)(1).[168] It would also allow issuers to increase the information value of roadshow presentations by permitting written material to be delivered during roadshows.[169]

On the other hand, the free writing filing requirement presents problems. It is unclear how filing will be possible for multimedia presentations because the new EDGAR II[170] system will be unable to accommodate multimedia.[171] In addition, some securities attorneys have argued that it will be extremely burdensome to file all free writing material and that the section 12(a)(2)[172] liability risks attached to the additional filings will result in an even greater shift to oral communications.[173] This shift may be further magnified because the Aircraft Carrier Release does not define "writing" for the purposes of the filing requirement. Consequently, companies may opt away from anything that may remotely be construed as a writing.[174]

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165. *Id.*

166. The Regulation of Securities Offerings, *supra* note 110, at *67,216.

167. *Id.* at *67,215.

168. *New Rules Would End Road Show No-Action Requests*, FIN. NET NEWS, Nov. 23, 1998, at 6; *construed in* Marson, *supra* note 100, at 303.

169. The Regulation of Securities Offerings, *supra* note 110, at *81,525.

170. EDGAR II is the documentation system proposed to replace EDGAR in the SEC's attempt to modernize its technology and transition to Internet technology. *See also* Letter from Kris Wiklund, EDGAR Advantage Operations Manager, Merrill Corporation and John Stolle, Vice President of Technology, Merrill Corporation, to Jonathan G. Katz, Secretary, Securities and Exchange Commission (Apr. 3, 2000), *available at* http://www.sec.gov/rules/proposed/s70500/wiklund1.htm (last visited Dec. 17, 2002).

171. *See supra* note 168.

172. 15 U.S.C.S. § 77(1) (2002).

173. Charles Sisk, *Street Ready to Take Shots at SEC Flagship*, CORP. FINANCING WK., Nov. 30, 1998, at 8, *construed in* Marson, *supra* note 100, at 304.

174. Marson, *supra* note 100, at 305.

2. E-mail and Other Internet Communications

The proposed rules would also allow issuers and market participants to use electronic mail to answer investors' questions about the company and its offering, conduct chat room discussions, and post offerings messages on bulletin boards.[175] However, it is not clear if or how issuers would file these materials with the SEC.

3. Corporate Web Sites

By allowing offers during the pre-filing period, the Aircraft Carrier Release eases large, seasoned issuers' concern that web site content could be interpreted as a solicitation for an offering. This enables the large seasoned issuers to feel more secure about advertising and providing information about upcoming offerings on their web sites.[176] Still, small issuers will have to "remove any materials not covered by the proposed safe harbours (i.e., 'factual business information' and 'regularly released forward-looking information') thirty days before filing."[177] And all issuers still must continue the costly monitoring of their web sites to avoid section 12(a)(2) and anti-fraud liability from hyperlinked material or postings.[178]

The question of whether the SEC would require third-party materials hyperlinked to a company web site to be filed as free writing, consistent with the envelope theory, remains unresolved.[179] If so, the SEC would have to determine (1) whether the requirements would be affected by the type of link between sites; (2) whether the third-party materials would have to be accompanied by language instructing investors to read the disclosure documents filed with the SEC; and (3) what parameters would guide a company's description of the third-party free writing material when the third party's web site is outside the control of the company and subject to change at any time.[180]

C. *Prospectus Delivery Requirements*

Under the Aircraft Carrier Release, the SEC would require prospectuses or term sheets to be delivered before investors make their investment

175. *See* The Regulation of Securities Offerings, *supra* note 110.
176. Marson, *supra* note 100, at 306.
177. *Id.*
178. *Id.*
179. *Id.* at 307.
180. *Id.*

decisions.[181] Refreshingly, unlike the current requirement under section 5(b)(2) of the 1933 Act for delivery at or before a sale is confirmed, the proposed revision is structured for the investor's protection.[182] Notably, some investment bankers argue that this proposed timing revision "will significantly slow down offerings by large issuers who currently can use the shelf registration system[183] to offer securities in a matter of hours."[184]

V. CONCLUSION

Offering securities to the public is a major event in the business life of any enterprise. The uncertainty surrounding market reception of an offering is an inherent risk, unnecessarily compounded by the ambiguities of Internet-related securities regulations. Among the issues that seem to impede the use of electronic media are some of the definitional issues, such as: (i) how an issuer is to know when the SEC will consider e-mail an oral communication and when it will consider it a written communication; (ii) what the status of issuer involvement is in interactive discussions, like forums, bulletin boards, message centers, and chat rooms, as these have restrictions on waiting period activities; (iii) the degree to which issuers will be liable for hyperlinked information; (iv) how often issuers are responsible for monitoring their web sites. On a daily basis? Hourly? Continuously?; (v) at what point and to what depth are issuers responsible for web site content. At each web page? For investigation of all hyperlinks? Initially or continuously?; (vi) how it is possible to have an electronic-only offering if the SEC requires paper disclosures on an investor's request; and (vii) whether a national offering is subject to the laws of every state.

The Internet has the potential to dramatically enhance the efficiency of securities offerings by increasing the speed of communications, expanding the availability of information to investors, and substantially reducing manual processes. Automating processes reduces errors, employee time spent performing administrative functions, and the mailing of information, consequently reducing cost. Reducing the cost of a securities offering in turn lowers the barrier to market entry, which encourages more businesses

181. Marson, *supra* note 100, at 307. According to the SEC, the procedural requirements of notice, access, and evidence of delivery discussed in the Securities Act Release No. 337,233 (Oct. 5, 1995) would still be applicable. *See* The Regulation of Securities Offerings, *supra* note 110.

182. *See id.*

183. *See* 17 C.F.R. § 230.415(a)(2) (2002). *See also* JENNINGS ET AL., *supra* note 16, at 270. Shelf-registration provides issuers the procedural flexibility to register securities that they plan to sell within two years from the effective date of the registration statement. *Id.* This allows issuers to time periodic offerings to be able to take advantage of favorable market conditions. *Id.*

184. Marson, *supra* note 100, at 303.

to engage the capital markets for their fundraising needs. The ultimate result is the promotion of business development, business growth, and total wealth. But until the SEC resolves these issues, the Internet's amazing power will not be fully utilized.