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Surfing the Web for Capital: The Regulation of Internet Securities Offerings

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The Internet is having a profound effect on all parts of the securities business: web sites are linking small companies with angel investors; growing companies are selling securities directly to the


1. Originally designed by the military to help computer scientists and engineers working on military projects communicate with one another, the loose collection of transmission lines, routers, and servers that comprise the Internet has now become a mass communication medium used by business, universities, individuals, and the government. Information is transmitted over the Internet via the World Wide Web, electronic mail, and electronic bulletin boards. For a general survey on the rise of the Internet, see The Accidental Superhighway, ECONOMIST, July 1, 1995, at 50.

2. Angel investors generally are individual investors or groups of individual investors who invest money in companies in exchange for stock when the company is not yet large enough to attract venture capital. Angel investors want a strong return on their investment, but may also have altruistic motivations as well. See Gwyneth E. McAlpine, Getting a Piece of the Action: Should Lawyers be Allowed to Invest in their Clients’ Stock?, 47 UCLA L. REV. 549, 571-72 (1999).
public over the Internet; large publicly traded corporations are conducting "roadshows" over the Internet and distributing annual reports, prospectuses, and proxy materials via their web sites; and retail investors are routinely trading securities using on-line services.  Each of these developments has raised a host of legal issues. The U.S. Securities and Exchange Commission (the SEC) must, in response, apply and adapt a regulatory framework that was created almost seven decades ago by the Securities Act of 1933 (the "Securities Act") and the Securities Exchange Act of 1934 (the "Exchange Act") to a securities industry that is rapidly integrating the Internet into its everyday practice. How it chooses to do so could have a profound affect on the future development of the capital raising process in the United States.

Congress passed the securities laws in response to the activities culminating in the 1929 market crash. The legislation created a regulatory scheme designed to ensure that securities offerings, as well as the listing and registration for public trading of such securities on a securities exchange, were accompanied by full disclosure of relevant information to the investing public. Under the Securities Act, companies intending to sell securities to the public must register the securities by filing a registration statement with the SEC. The registration statement, which includes the statutory prospectus sent to investors, contains the information about the company and the

3. For general discussions on the rise of Internet web sites involved in securities offerings, see Constance E. Bagley & Robert J. Tomkinson, Internet is Seeing its Share of Securities Offerings, Nat'L L. J., Feb. 2, 1998, at C3 (predicting that the Internet will become an alternative to traditional means of raising capital); Richard Raysman & Peter Brown, Securities Offerings Over the Internet, N.Y. L.J., June 10, 1997, at 3 (noting that Internet-based securities offerings are likely to increase, especially for smaller companies that do not have access to institutional investors or venture capital). But see Andrew Reinbach, Internet IPOs: Hip or Hype?, AM. BANKER, Nov. 10, 1997, (Future Banker Magazine), at 40 (arguing that the attention given to Internet-based offerings is much larger than their actual performance, and that most large banks are unlikely to participate due to high risks and low returns).


6. A central question in many areas of the law is whether existing legal regimes can be adapted to the problems presented by new technologies or whether new regimes will need to be created. On this issue as it relates to securities regulation and the Internet, see Robert A. Prentice, The Future of Corporate Disclosure: The Internet, Securities Fraud, and Rule 10b-5, 47 EMORY L.J. 1, 7 (1998) (arguing that existing antifraud statutes and rules can be adapted to Internet abuses).

7. See 15 U.S.C.A. § 77e(a), (c) (West 1997).
offering that investors would need to properly evaluate the security.\(^8\)

This paper focuses principally on the ways in which these registration
and disclosure requirements of the Securities Act apply to offerings
conducted over the Internet, the relevant exemptions from these
requirements, and the potential effect of recent reform efforts on
Internet-based securities offerings.

Part One reviews the current approach to the regulation of
Internet-based securities offerings. It first examines the SEC’s
approach to securities offerings conducted over the Internet that are
exempt from the registration requirements of the Securities Act. It
then examines the regulation of registered public offerings, focusing
on the requirements for electronic delivery of information. Finally, it
analyzes the rules regarding Internet-based roadshows. Part Two
examines the SEC’s most recent reform proposal, “The Aircraft
Carrier Release,” so-called because of its enormous size. It first
reviews the basic provisions of the Release, and then highlights the
probable impact of the proposed changes on Internet-related securities
offerings. Part Three concludes, arguing first that the Release
provides insufficient guidance to companies conducting exempt
offerings over the Internet and, second, that the Release should be
revised, specifically by eliminating the requirement that “free
writings” be filed with the SEC, so as to encourage the use of the
Internet as a means for information delivery.

I. CURRENT LAW

   A. Exempt Offerings

   Small companies face disproportionately high expenses in a
registered public securities offering because many of the activities
required by the securities laws, such as putting together a prospectus
and mailing information to investors, are relatively fixed costs. In
addition, because they have never accessed the public markets before,
compliance with the disclosure requirements of the securities laws
often requires small companies to reorganize their capital structure,
employ auditors, and gather significant amounts of information about
the company for the first time. Thus, the costs of a registered public
securities offering may be far too great for a small or growing
company that requires only a minor amount of capital.\(^9\)

9. See Stephen J. Choi, Gatekeepers and the Internet: Rethinking the Regulation of Small
Fortunately, these companies can take advantage of several exemptions from the registration requirements of the federal securities laws. In particular, section 3(b) of the Securities Act authorizes the SEC to add any class of securities to the general list of those exempted by section 3, subject to certain restrictions, provided that the aggregate amount offered is less than $5 million. Exemptions under section 3(b) include Regulation A and Regulation D, Rules 504 and 505. In addition, section 4(2) provides a private placement exemption for transactions not involving any public offering. Regulation D, Rule 506 provides a safe harbor under this Section for offerings of unlimited size, provided that they are sold only to accredited or sophisticated investors, and that sales are not made to more than thirty-five non-accredited investors. Offerings under Rules 505 and 506 must meet the general conditions of Rule 502, including a prohibition on general solicitation and advertising, information and delivery requirements, and limitations on resale.

1. Regulation D and General Solicitation — Issuers conducting offerings over the Internet relying on the exemptions under Rules 505 or 506 of Regulation D must be careful not to engage in general solicitation or advertising prohibited by Rule 502(c). The SEC has made it clear that, in the context of an exempt offering, the placement of offering materials on an Internet web site without sufficient procedures to limit access to accredited investors is inconsistent with the prohibition against general solicitation or advertising. For example, if a company raising money through a private placement pursuant to Rule 506 simply placed its offering materials on its Internet site without restricting access to the materials beyond

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10. See 15 U.S.C.A. § 77c(a), (b) (West 1997).
12. Id. §§ 230.504, 230.505.
14. Accredited investors include individuals with a net worth exceeding $1 million dollars or an annual income exceeding $200,000 (or $300,000 including the individual's spouse), as well as various institutions such as banks, broker-dealers, and insurance companies. See Securities Act Rules, 17 C.F.R. § 230.501(a) (1999).
15. A sophisticated investor is an investor having "such knowledge and experience in financial and business matters that he is capable of evaluating the merits and risks of the prospective investment." Such an investor may be sophisticated alone or with a purchaser representative. See id. § 230.506(b)(ii).
16. See id. § 230.506.
17. See id. § 230.502.
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requiring certain information, it would be engaging in prohibited general solicitation.\textsuperscript{19} Therefore, if an on-line service is involved in offerings exempt under Rules 505 or 506 of Regulation D, it must place restrictions on the ability of potential investors to view such material, or it must otherwise locate prospective purchasers without a general solicitation.

In a no-action letter to IPONet, the SEC’s Division of Corporation Finance approved a restricted access web site as consistent with the prohibition of general solicitation and advertising under Regulation D in the context of Internet-based private offerings.\textsuperscript{20} Persons who have registered with IPONet can request registration as an accredited or sophisticated investor by filling out an on-line questionnaire designed to allow the company to determine whether the member is an accredited investor within the meaning of Rule 501(a) of Regulation D or a sophisticated investor under Rule 506. Once a member is qualified as either an accredited or sophisticated investor, he is given a password allowing him access to a restricted page where private offerings are posted.\textsuperscript{21} The Division of Corporation Finance wrote that the qualification of investors through the use of a questionnaire would not constitute general solicitation or advertising provided that three conditions were met: (1) both the invitation to complete the questionnaire and the questionnaire itself do not reference any specific transactions posted or to be posted on the password protected page; (2) the password protected page is only available to an investor after the company has determined that he is accredited or sophisticated; and (3) the investor is only able to purchase securities in transactions that are posted after the investor is qualified with IPONet.\textsuperscript{22} Thus, the posting of a notice of a private offering on a web site would not be deemed a public solicitation or general advertisement within the meaning of Regulation D when pre-qualification and password-protection procedures designed to limit access to the web site to accredited and sophisticated investors are in place.

The purpose of the IPONet no-action letter’s third condition, that investors can only purchase securities posted after the investor has been qualified, is to ensure that investors do not join an on-line

\textsuperscript{19} See id. at 3131-7.
\textsuperscript{21} See id. at 77,272.
\textsuperscript{22} See id. at 77,274.
service in order to invest in a particular offering. The SEC further refined this condition in its no-action letters to Lamp Technologies, Inc. ("Lamp"). Lamp lists descriptive information and performance related data from hedge funds that are privately offered pursuant to Regulation D. Subscribers to the password protected site—generally sophisticated investment and financial professionals—are pre-qualified by Lamp as accredited investors through the use of a questionnaire. Because hedge funds have continuous quarterly or annual sales, rather than requiring investors to invest only in funds posted after their qualification, Lamp imposes a thirty-day waiting period during which time subscribers cannot invest in any posted hedge fund (other than funds in which the subscriber already invests, for which he has already been solicited, or in which he is already actively considering an investment). The Division of Corporation Finance approved this procedure, noting that Lamp would not be considered to be engaging in general solicitation or advertising provided it meets the first two conditions of the IPONet no-action letter and enforces its thirty-day waiting period in lieu of the condition that investors can only purchase securities posted after the investor has been qualified.

The opportunity for small companies to directly tap capital sources by using the Internet rather than traditional investment advisory services has produced a phenomenon recently dubbed "technological disintermediation." Until recently, in order not to violate the prohibition on general solicitation, small companies had to

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24. Hedge funds are largely unregulated private investment companies, usually in the form of partnerships, limited liability companies, or offshore corporations, that use a variety of alternative investment techniques, such as short-selling and derivatives. They may or may not use "hedging" strategies. See Leon M. Metzger, Recent Market Events and the Foundation for Global Market Crises: Hedge Funds, 4 FORDHAM FIN. SEC. & TAX L.F. 5, 6 (1999).


26. See id.

27. See id. at 77,806.


29. See Donald Langevoort, Angels on the Internet: The Elusive Promise of "Technological Disintermediation" for Unregistered Offerings of Securities, 2 J. SMALL & EMERGING BUS. L. 1, 2-3 (1998) (noting that "[t]echnology raises the promise of a substantially disintermediated capital market for start-up business, wherein entrepreneurs are able to solicit capital without having to pay underwriters or broker-dealers for marketing services, or lawyers and accountants for the heavy expenses associated with a registered public offering.") (footnote omitted).
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undergo the cumbersome and expensive task of first finding qualified investors, and then after some period of time contacting them with a specific investment proposal. This process would almost always require the assistance of an investment professional or registered broker-dealer that had already compiled a list of pre-qualified investors through mailings, telephone solicitations, or personal contacts. With the rise of Internet-based systems like that of IPONet, however, companies can now directly access lists of prospective investors without the need for investment professionals. Thus, technology has eliminated the need for the "intermediary." Proponents of this phenomenon have argued that it substantially reduces the costs of raising capital for small businesses who can reach a large audience of potential investors without having to pay broker-dealers fees for marketing their company, and without having to sacrifice the extensive legal, accounting, and investment banking costs associated with a registered offering.

2. Information Delivery and the Number of Purchasers — Other potential problems that could arise should an on-line service participate in offerings under Rules 505 or 506 of Regulation D without restricting access to accredited investors relate to information delivery requirements and restrictions on the number of purchasers. Rule 502(b) requires that certain information be furnished if issuers

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30. See id. at 7.
31. Section 3(a)(4) of the Exchange Act defines a broker as "any person engaged in the business of effecting transactions in securities for the account of others." 15 U.S.C.A. § 78c(a)(4) (West 1997). Under § 3(a)(5) of the Exchange Act, a dealer is "any person engaged in the business of buying and selling securities for his own account, through a broker or otherwise." Id. § 78c(a)(5). By collecting orders and executing them in the various securities markets, broker-dealers facilitate securities trading. Exchange Act § 15(a) requires brokers and dealers to register with the SEC. See id. § 78o(a).
32. See Langevoort, supra note 29, at 7.
33. See id. at 7–8.
34. See id. at 3. Critics of the disintermediation of capital markets have argued that the process compounds information asymmetry problems between investors and companies and, by allowing small firms to shift their sources of capital from traditional financing methods (such as bank loans, venture capital, and angel investors) to public capital markets, the process increases monitoring costs. See, e.g., Bernard Black, Information Assymetry, the Internet, and Securities Offerings, 2 J. SMALL & EMERGING BUS. L. 91, 91 (1998) (arguing that "the Internet could increase information assymetry costs by undercutting the effectiveness of the institutions that today provide investors with partial assurance of the quality of the information provided by issuers."); Jill Fisch, Can Internet Offerings Bridge the Small Business Capital Barrier?, 2 J. SMALL & EMERGING BUS. L. 37, 57 (1998) (arguing that there are "nonfinancial benefits that banks and private equity provide to small businesses through active managing and monitoring" and that "[s]hifting the source of small business capital may sacrifice these benefits, at the costs of future business performance.").
sell securities under Rules 505 or 506 to non-accredited investors.\textsuperscript{35} If the on-line service is acting as a broker-dealer and selling the securities itself, such information would need to be furnished to everyone accessing the site, since there would be no way to determine whether the person purchasing such securities is accredited or not. If the on-line service is merely posting the offering materials and requires an investor to contact the issuer directly to purchase any securities, the service could presumably rely on the issuer to provide the required information before conducting a sale. However, because Rule 502(b)(1) requires such information to be provided to all non-accredited investors “a reasonable time prior to sale,” it is safer to furnish the information initially on the web site.\textsuperscript{36}

Rules 505(b)(2)(ii) and 506(b)(2)(i) require offerings to be limited to no more than thirty-five non-accredited investors.\textsuperscript{37} Depending on how the on-line service functions, a service selling securities may not be able to restrict sales to only thirty-five non-accredited investors. Furthermore, even if it could, the service may be forced to unduly restrict the number of potential sales by selling to a total of only thirty-five purchasers (whether accredited or not) to prevent violating the limitation on the number of non-accredited investors. Again, a service merely providing information could presumably rely on the issuer to determine accredited status and restrict the number of sales to non-accredited investors to thirty-five.

3. Regulation A — Regulation A provides an exemption from registration for offerings of up to $5 million, imposes no limits on the number of offerees or purchasers, and authorizes the use of some forms of advertising.\textsuperscript{38} Issuers taking advantage of Regulation A must, however, file an “offering statement” with the SEC, which includes an “offering circular” that must be delivered to purchasers prior to sale.\textsuperscript{39} Regulation A offerings have been dubbed “minipublic” offerings because the information required to be disclosed in the offering statement is similar to, though far less extensive than, that mandated to be included in a registration statement.\textsuperscript{40}

Because Regulation A offerings (as well as those conducted

\textsuperscript{36} Id. § 230.502(b)(1).
\textsuperscript{37} See id. § 230.505(b)(2)(ii), 230.506(b)(2)(i).
\textsuperscript{38} See id. § 230.251.
\textsuperscript{39} See id.
\textsuperscript{40} See MARC STEINBERG, UNDERSTANDING SECURITIES LAW 54–55 (2nd ed. 1996).
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pursuant to Rule 504 of Regulation D) are not subject to restrictions on public solicitations or advertising, some web sites involved in Internet-based offerings have limited the types of unregistered offerings they post to those exempt under Regulation A. For example, in its request for no-action letter assurance, the Internet Capital Corporation ("ICC") explained that it does not list offerings exempt under Rules 505 or 506. ICC's user registration process only requires that the potential investor provide his name, address, state of residence, and electronic mail address. While ICC will validate this information, unlike IPONet it has no procedure for determining whether an investor is accredited or not. In a no-action letter, the Division of Corporation Finance approved this electronic posting of offering materials.

A second attractive feature of Regulation A is the fact that issuers are allowed to "test the waters" to determine if there is any potential investor interest in a proposed offering. Specifically, issuers can publish or deliver "solicitations of interest" to potential investors consisting of oral communications, written documents, or radio or television broadcasts about the company and the offering. This ability to "test the waters" has made Regulation A particularly attractive to small companies intending to sell securities directly to the public without the aid of an underwriter in so-called "direct public offerings." For example, Spring Street Brewing Company, which conducted the first ever Internet-based direct public offering, placed an offering circular complying with the requirements of Regulation A on its web page along with an investor subscription agreement that investors could complete and return with a check to purchase securities from the company. The company raised $1.6 million and avoided underwriting fees entirely.

B. Registered Public Offerings

The SEC has generally encouraged the use of electronic distribution methods for transmitting required information to

41. See Internet Capital Corp., SEC No-Action Letter, 1997 WL 796944 (S.E.C.), at *1 (Dec. 18, 1997). ICC posts both registered and unregistered offerings. However, the only unregistered, i.e. exempt, offerings it posts are Regulation A and SCOR offerings. See id.
42. See id. at *3-*4.
43. See id. at *5.
investors, and clearly expects the use of electronic media to grow in popularity in the securities industry. One reason for this inevitable growth is that the preparation and delivery of documents in a registered public offering, from the prospectus to sales literature and research material, can be accomplished at significantly less cost by using the Internet rather than traditional paper-based methods.\(^4\) Other benefits of electronic delivery include much greater speed and the leveling effect of ending the current two-tiered system of disclosure that often allows larger institutional shareholders to receive information before smaller retail investors.\(^4\)

Section 5(b)(2) of the Securities Act requires that a prospectus containing the salient data set forth in the registration statement be delivered to any investor purchasing a security either before or at the time of sale.\(^4\) This requirement is designed to ensure that investors are given the information they need to properly evaluate the security and to make an informed investment decision. Thus, a central question is to what degree issuers can rely on the Internet to meet this disclosure obligation by transmitting the required information electronically.\(^4\) The SEC's general approach is that information distributed through electronic means satisfies the transmission requirements of the securities laws as long as the intended recipients receive substantially the same information as they would have received if the information had been delivered to them in paper

\(^{46}\) See McGlosson, supra note 45, at 315.

\(^{47}\) See Catherine M. Kilbane, Prospectus Delivery via the Internet, 8 CORP. ANALYST 62, 63–64 (1996). Institutional investors, by virtue of the fact that they usually possess "significant assets and expertise," are generally assumed to be in a position to demand information from issuers similar to what might be included in a registration statement. Kenneth Denos, Blue and Gray Skies: The National Securities Markets Improvement Act of 1996 Makes the Case for Uniformity in State Securities Law, 1997 UTAH L. REV. 101, 120 (1997). Such institutional investors include insurance companies, various forms of investment companies, pension plans, dealers, investment advisors, and certain charitable organizations. See id. at 121. Already some leveling has been accomplished by the SEC's web site. See David M. Cielusniak, You Cannot Fight What You Cannot See: Securities Regulation on the Internet, 22 FORDHAM INT'L L.J. 612, 617 (1998) (noting that the use of EDGAR for Exchange Act filings has made extensive financial information about public companies instantly available to any investor via the SEC's web site).

\(^{48}\) Section 5(b)(2) of the Securities Act makes it unlawful to "carry or cause to be carried through the mails or in interstate commerce any such security for the purpose of sale or for delivery after sale, unless accompanied or preceded by a prospectus that meets the requirements of subsection (a) of section 10." 15 U.S.C.A. § 77e(b)(2) (West 1997).

This section reviews the SEC’s three guiding principles for electronic delivery: notice, access, and evidence of delivery.

1. **Notice** — Parties using electronic delivery must ensure that their electronic communication provides timely and adequate notice to investors that information regarding a proposed offering is publicly available. While the delivery of an electronic document itself (such as a CD-ROM or an electronic mail) constitutes sufficient notice, posting a document on an Internet web site, without separate notice, does not satisfy the delivery requirements. In general, notice by publication in a newspaper, bulletin board, or web site is also insufficient.

If, however, an investor has consented to electronic delivery via a web site, a note with the confirmation of sale of the security indicating that the final prospectus is available on a web site is sufficient to satisfy the delivery requirements. Moreover, if such an investor has provided his or her electronic mail address for the purpose of being notified, an issuer may send notice of the location of the final prospectus via electronic mail. Assuming again that an investor has consented to electronic delivery, notice can be given by including in the forepart of a company's sales literature a clearly highlighted provision indicating the availability on an Internet web site of the final prospectus.

2. **Access** — Electronically delivered information must provide investors with comparable access to the required disclosure information as would a conventionally delivered paper document. Thus, the electronic medium cannot be "so burdensome that intended recipients cannot effectively access the information provided." For example, if an investor must navigate through a confusing series of

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50. See October Release, supra note 18, at 3131.
51. See id. at 3131-2.
52. See id. at 3131-7. In some circumstances, the issuer will be able to show that delivery to an investor has been satisfied by other means or that the document is not required to be delivered. For example, in an offering, neither notice of the availability of an updated or final prospectus nor the updated or final prospectus itself need be sent, through any means, to persons who have already received an electronic preliminary prospectus, but to whom securities are not expected to be sold. See id. at 3131-2 n.23.
53. See id. at 3131-3. Investors who have not consented to electronic delivery via a web site cannot be presumed to be able to access the web site; thus, a note indicating availability of the final prospectus on the web site is insufficient without such consent. See id.
54. See id. at 3131-5.
55. See id. at 3131-6.
56. See October Release, supra note 18, at 3131-2.
57. Id.
menus to access a document so that it is unreasonable to expect the investor to gain access, the procedure would be viewed as too burdensome and delivery would not be deemed to have occurred.\textsuperscript{58} However, a procedure for ensuring access to prospectuses and other material that serves to limit access to all the materials to those with user identification numbers (even if the process of getting an identification number requires significant information and time from the investor) is not considered to be overly burdensome.\textsuperscript{59} Such burdens are considered to be "part of the process of providing access to all the information, including supplemental sales literature, and not to be a unique burden upon access to the prospectus."\textsuperscript{60}

On-line viewing is not a "prerequisite to electronic delivery."\textsuperscript{61} Thus, a prospectus made available on the Internet that requires downloading of the entire document can still satisfy the delivery requirement.\textsuperscript{62} In any case, since the investor must have the opportunity individually to "retain the information or have ongoing access equivalent to such personal retention," an issuer should at least allow, and perhaps even require, an investor to download the information.\textsuperscript{63} "[T]he document should also be accessible for as long as the delivery requirement applies."\textsuperscript{64}

Documents required to be accompanied by one another must each be as accessible as the other. Consider a web site that contains a prospectus and an application for a mutual fund as two separate files that can be downloaded independently. If an investor must download special software to view the prospectus but not the application, even a statement in a returned and completed application that the investor received the prospectus is insufficient to evidence electronic delivery of the prospectus.\textsuperscript{65} On the other hand, if "it is not significantly more burdensome to access the prospectus than the application form (e.g., no additional software is necessary to read either document . . . )," and the user downloads them together (even if they become two

\textsuperscript{58} See id. at 3131-2 n.24.
\textsuperscript{59} See id. at 3131-10.
\textsuperscript{60} Id.
\textsuperscript{61} Id. at 3131-11.
\textsuperscript{62} See October Release, supra note 18, at 3131-10 to 3131-11.
\textsuperscript{63} Id. at 3131-2.
\textsuperscript{64} Id. at 3131-2. In general, the prospective delivery requirement for sales other than from an unsold allotment lasts for 25 days after the offering date, which is defined as the date on which the registration statement becomes effective or the date on which the securities were bona fide offered to the public. See Securities Act Rules, 17 C.F.R. § 230.174 (1999).
\textsuperscript{65} See October Release, supra note 18, at 3131-9.
Last, because of possible system failures, incompatibilities, and revocations of consent, issuers must be able to deliver a paper version of documents delivered electronically. In particular, an issuer must provide a paper version of a document if a person revokes his consent to receive a document electronically or specifically requests a paper version. The SEC noted that this requirement should not preclude an issuer from structuring its offering through only electronic communication, but cautioned that the issuer must still deliver information through paper if electronic means can no longer be relied upon to deliver information required to be provided by the securities laws.

3. Evidence to show delivery — Issuers or broker-dealers can obtain direct evidence that a particular investor actually received required disclosures by electronic mail, return receipts, or by confirmation that the investor accessed, downloaded, or printed the document. Direct evidence of receipt may also be obtained through evidence that an investor has used other materials that are only available once the investor has already accessed the required disclosure information. However, obtaining an informed consent from an investor stating that the investor specifically consents to receive information through a particular electronic medium obviates the need to produce direct evidence of delivery altogether. Informed consent requires that investors be apprised of the particular electronic medium to be used (e.g., a web site), potential costs (such as on-line time), and “the period during and documents for which the consent will be effective.”

Even without an explicit consent, the SEC has made it clear that an investor accessing a required document via the Web can evidence

66. Id.
67. See id. at 3131-2.
68. See id. An investor need not withdraw his consent to request a paper copy of a document. See id. at 3131-8.
69. See id. at 3131-2 n.27.
70. See id. at 3131-3.
71. See October Release, supra note 18, at 3131-3.
72. See id.
73. Id. at 3131-3 n.29. An issuer can rely on a consent given to an underwriter, brokerage firm, or other service provider, and vice versa. See id. Such a consent must, however, specifically indicate that the investor consents to delivery of future documents by the particular electronic medium. See id. at 3131-4.
delivery of the required document. For example, because sales literature must be preceded or accompanied by a final prospectus, such material, if placed on a web site, must include a hyperlink to the final prospectus. In this case, "the hyperlink function enables the final prospectus to be viewed directly as if it were packaged in the same envelope as the sales literature," a notion called the "envelope theory." Alternatively, sales material can be placed on the same menu as the prospectus as long as the two are clearly identified and in close proximity to one another.

The SEC's analogy between two hyperlinked documents and the inclusion of the two documents in the same envelope can create pitfalls for issuers. For example, during the "waiting period," the time between the filing of the registration statement and the date on which it is deemed effective, section 5(b)(1) prohibits any written communications relating to the security offering unless made through the use of a prospectus conforming to the strict informational requirements of section 10. Thus, issuers must be careful not to provide direct access via a hyperlink from their preliminary prospectus to research reports since such reports most certainly do not meet the information requirements of section 10. In several no-action letters, the SEC has allayed issuers' concerns that the reference in a prospectus to an issuer's filings on its web site would incorporate by reference all other material on the site, such as marketing material. An issuer may, therefore, include in its prospectus a statement such as, "our SEC filings are also available to the public

74. See id. at 3131-4.
75. See id. at 3131-6.
76. Id.
77. See October Release, supra note 18, at 3131-6. The envelope theory seems only to apply to hyperlinks, and not to less speedy connections between documents. For example, a web site that allows a user to click on a box displayed in the supplemental sales literature to have the prospectus downloaded or to request that one be mailed, but does not allow the prospectus to be viewed on-line, "would not satisfy the prospectus delivery requirement... because the system does not give users reasonably comparable access to the prospectus and the sales literature .... " May Release, supra note 49, at 3131-23.
78. See October Release, supra note 18, at 3131-5 to 3131-6.
79. Section 5(b)(1) of the Securities Act makes it unlawful to "transmit any prospectus relating to any security with respect to which a registration statement has been filed... unless such prospectus meets the requirements of section 10." 15 U.S.C.A. § 77e(b)(1) (West 1997).
80. See October Release, supra note 18, at 3131-6.
from our web site,”82 without incorporating information other than the Exchange Act filings, such as documents available through hyperlinks from the company’s main site.83

C. Internet Roadshows

Roadshows have become an integral part of securities offerings. Roadshows usually consist of a series of meetings at which the issuer’s management makes presentations to institutional investors, securities firms, trading and sales personnel, and research analysts. A roadshow allows the underwriters to present information concerning the merits of the upcoming securities offering and the future prospects of the issuer, and provides an opportunity for potential investors to ask questions.84 Roadshows take place during the waiting period.85 During this period, section 5(b)(1) of the Securities Act prohibits the use of any prospectus other than a prospectus meeting the informational requirements of section 10 in order to market the securities.86 Section 2(a)(10) defines a prospectus broadly as any “prospectus, notice, circular, advertisement, letter, or communication, written or by radio or television, which offers any security for sale.”87 Since roadshows are essentially oral presentations, they do not fall within this statutory definition of a prospectus, and are thus not subject to section 5(b)(1). Until recently, however, the reference to radio and television in section 2(a)(10) foreclosed the use of electronic communications to transmit oral roadshows for fear that such communications would be considered prospectuses.88

In a no-action letter to Private Financial Network (“PFN”),89 the

82. Baltimore Gas, supra note 81, at *2.
83. See id.
85. Roadshows cannot be conducted in the “pre-filing period,” the time before a registration statement has been filed, because § 5(c) of the Securities Act prohibits all offers to sell a security unless a registration statement has been filed with the SEC. 15 U.S.C.A. § 77e(c) (1997). The term “offer to sell” is broadly defined in § 2(3) of the Securities Act to include “every attempt to offer or dispose of” a security, and has been interpreted broadly to include any publicity intended to condition the market for a public offering. See HAROLD S. BLOOMENTHAL ET AL., SECURITIES LAW HANDBOOK § 5.01(2) (1999).
87. Id. § 77b(a)(10).
89. PFN, a subsidiary of the MSNBC joint venture between NBC and Microsoft, provides
Division of Corporation Finance approved PFN’s proposal to transmit roadshow presentations to its subscribers via satellite, T1 telephone lines, and cable under the assumption that such communications would not fall under the definition of a prospectus within the meaning of § 2(a)(10) of the Securities Act. \(^{90}\) PFN argued that an electronic roadshow would not lose its character as an “oral” presentation merely because it is transmitted over the same technology as radio or television. \(^{91}\) Indeed, the reference to radio and television in § 2(a)(10), PFN argued, was “intended to prevent mass communications to the public unaccompanied by the sort of disclosure required § 10.” \(^{92}\) Citing *Gustafson v. Alloyd Co., Inc.*, \(^{93}\) PFN argued that the term “prospectus” was only meant to refer to communications widely disseminated to the public rather than to a smaller, invited audience. \(^{94}\) The SEC granted the no-action letter with little commentary. \(^{95}\)

Subsequently, the SEC has granted several no-action letters to other companies providing electronic roadshows. In particular, the Commission has provided no-action letters to two companies transmitting roadshow presentations over the Internet: Net Roadshow and Thomson Financial Services’ Virtual Roadshow. \(^{96}\) Both services operate in much the same way as PFN, except that they broadcast their roadshow presentations over the Internet. On Net Roadshow’s web site, anyone can view the list of roadshows and underwriters, but

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90. *See id.* at 77,678.
91. *See id.* at 77,676.
92. *Id.* at 77,677.
95. *See id.* at 77,678. PFN does take several steps to ensure compliance with the securities laws, such as making the transmissions available only to the network’s subscribers, who must agree not to tape, copy, or further distribute the presentation, and insuring that each subscriber receives a prospectus before a roadshow is transmitted. In addition, PFN instructs issuers and underwriters to make sure that the information disclosed in the roadshow is not inconsistent with the information contained in the prospectus, and includes with each transmission a visual statements (or “crawl”) emphasizing the primacy of the prospectus as well as the prohibition on copying and further distribution. *See id.* at 77,676 – 77.
an investor who wishes to view a particular presentation must contact one of the underwriters to obtain an access code, which is changed each day to prevent multiple viewings.97 Only qualified users with an identification number can access the Virtual Roadshow site’s index of companies. In order to view a roadshow presentation, a user must also have received authorization from the underwriter, who has previously agreed to provide a copy of the prospectus to investors before granting them such authorization.98 Although investors on Net Roadshow do not actually receive a paper prospectus before viewing the roadshow, investors are directed to access and download the prospectus through a prominently displayed button on the web page at any time before, during, and after the roadshow presentation.99

It is not entirely clear how far Internet-based roadshow providers can go in terms of expanding the audience for their presentations beyond institutional investors. On the one hand, if an electronic roadshow is by definition an oral communication, it should not matter how many or what kind of investors watch as long as adequate disclosure mechanisms are in place.100 On the other hand, all of the services receiving no-action assurance so far restrict their web sites to the types of investors who are ordinarily invited to roadshows, such as institutional investors or research analysts.101 Furthermore, a web site open to anyone could perhaps be analogized to broadcast media such as radio and television, which are explicitly part of the definition of a prospectus under section 2(a)(10), because any potential investor could “tune in.” The SEC has taken a few tentative steps in the direction of expanding the potential base of investors able to access Internet roadshows, such as by issuing a no-action letter to the heavily subscribed Bloomberg service to conduct electronic roadshows.102

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98. See Thomson Financial Services, supra note 96, at *5-*6.
99. See Net Roadshow, supra note 96, at 77,849. Similarly, Virtual Roadshow’s index has a hyperlink to the EDGAR system on the SEC’s web page. See Thomson Financial Services, supra note 96, at *5.
100. Cf. Quinn & Jarmel, supra note 88, at 4 (“Moreover, there is no legal limitation on the number or nature of potential investors that may attend or participate in such meetings. A company, for example, could, consistent with the Securities Act, hold a roadshow at Yankee Stadium.”).
More recently, the SEC gave oral assurances to Net Roadshow that it could expand its service to accredited individual investors, allowing them to tap into the increasing number of retail investors who invest on-line.\textsuperscript{103} The lack of guidance in this area, however, means that Internet roadshows may still be limited to certain types of investors, preventing the information contained in the presentations from directly reaching a broader audience.

II. PROPOSED CHANGES

The SEC has recently proposed significant changes to the regulatory framework established by the securities laws in what has been dubbed, "The Aircraft Carrier Release."\textsuperscript{104} While past reform efforts have usually been precipitated by a major event, such as the depression of the 1930s or the insider trading scandals of the 1980s, the issuance of the Aircraft Carrier Release does not seem to have been driven by any one factor, though the rapid growth in information technology and the rise of the Internet in particular have played an important role in the SEC's recent shift toward the deregulation of information delivery requirements.\textsuperscript{105} The SEC's stated goal of this reform effort is to increase the flexibility of registered offerings in terms of timing and disclosure without compromising investor protection.\textsuperscript{106} To this end, the Aircraft Carrier Release proposes to streamline the registration process for securities offerings, especially for seasoned issuers, while at the same time increasing the application of antifraud and civil liability protections for investors.

A. Introduction to the Aircraft Carrier Release

The proposed reforms would replace the current registration

1, 1997); BLOOMENTHAL ET AL., supra note 85, at § 5.02(b) (concluding that the Bloomberg no-action letter implies that the number of viewers is not important to the SEC).


105. See "Aircraft Carrier" Sprouts Leaks, INV. REL. BUS., Jan. 18, 1999 ("[T]he sweeping nature of the aircraft carrier proposal appears to be driven by the SEC's agenda, rather than a reaction to a major event."); Laura S. Unger, The "Aircraft Carrier": Technological Implications and Unresolved Issues, INSIGHTS, Jan. 1999, at 32 ("Technology—particularly the Internet—has made it easier to deliver information to investors. As a result, the Commission has rethought how improved information delivery impacts what information investors should have during the various stages of a securities offering.").

106. See Reform Release, supra note 104, § I(A), at 81,467.
statement forms with three new forms: Form A for small or unseasoned issuers; Form B for large, seasoned, and well-followed issuers or for offerings to sophisticated or informed investors; and Form C for business combinations and exchange offers. Form B registration statements would be deemed effective at the issuer's request, and would not be reviewed in advance by the SEC staff. Form B registration statements would also incorporate an issuer's Exchange Act filings by reference. As a tradeoff for the added flexibility and control over timing, however, Form B registrants would be required to include all transaction information within the registration statement prior to the first sale rather than in a supplement after sales are already made. Form B would generally be available only to issuers with a demonstrated market following. However, to encourage the registration of offerings to institutions that would otherwise be exempt from registration under Securities Act Rule 144A, the SEC has also proposed that Form B be available for sales to "qualified institutional buyers."

Issuers using Form A would have less flexibility than those using Form B. The rules governing effectiveness and incorporation depend, however, on whether an issuer is considered "seasoned" or not.

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108. See Reform Release, supra note 104, § V(A)(I)(d), at 81,478-79. In comparison, under the current system, it typically takes "several weeks to have a registration statement that is reviewed by the SEC declared effective." Marilyn Mooney & Gillian McPhee, Aircraft Carrier Proposals Change the Timing Of the Registered Offering Process, INSIGHTS, Jan. 1999, at 9.


111. See Reform Release, supra note 104, § V(A)(2)(a), at 81,481. Issuers considered to have such a market following must have both a history of reporting under the Exchange Act and either (1) a public float of between $75 and $250 million and an average daily trading volume of at least $1 million, or (2) a public float of above $250 million. See id. The SEC chose these criteria because it believes that they are the "most accurate measurement to attain the goal of choosing issuers for which there is an efficient market . . . ." Id.

112. Id. § V(A)(2)(b), at 81,482-83-84. Rule 144A provides an exemption from the requirements of Section 5 for the private resale of securities to certain institutions that are deemed to be "qualified institutional buyers," including insurance companies, employee investment plans, dealers, and banks. Securities Act Rules, 17 C.F.R. § 230.144A (1999).

113. For the purposes of allowing incorporation by reference, an issuer is considered to be seasoned if it has either (1) been a reporting company for at least two years and has a public float of over $75 million, or (2) has been a reporting company for at least two years and has
Issuers considered seasoned for the purposes of Form A would be able to incorporate their Exchange Act filings by reference into the prospectus in order to meet the company information disclosure requirements. These Form A registration statements would also be deemed effective at the seasoned issuer’s request. Unseasoned issuers and those conducting initial public offerings, on the other hand, would have to provide company-related information in full in the prospectus, and their Form A registration statements would be declared effective only after SEC review on the timetable of current S-1 registration statements.

The Aircraft Carrier Release would also significantly liberalize the rules restricting issuer communications during both the “pre-filing period,” the time before the issuer files a registration statement, and during the waiting period. Currently, section 5(c) of the Securities Act prohibits offers during the pre-filing period (the “gun jumping” restrictions), and section 5(b)(1) prohibits any written (though not oral) communications relating to a security offering during the waiting period unless made through the use of a prospectus conforming to the requirements of section 10(b). Under the Aircraft Carrier Release, all restrictions on offering communications during the pre-filing period would be removed for Form B registrants, allowing such issuers to make offers before filing a registration statement. Form A registrants could freely engage in offering communications up to the period starting thirty days before the date of filing of the registration statement. Moreover, during this thirty day “cooling off” period, all Form A issuers could release “factual business communications” and reporting companies using Form A could release “regularly released forward-looking information” as well. During the waiting period, the Aircraft Carrier Release would
allow issuers to make offers and communicate information in any form without having to meet the informational requirements of section 10. However, issuers would be required to file all such "free writing material" with the SEC.

In exchange for the accelerated timetable for offerings and increased flexibility regarding communications, the Aircraft Carrier Release clarifies and strengthens statutory antifraud and civil liability protections for investors. In particular, the Aircraft Carrier Release makes it clear that civil liability under section 11 of the Securities Act would apply to all information in the registration statement, including Exchange Act filings incorporated by reference. In addition, civil liability under section 12(a)(2) of the Securities Act would apply to all free writing materials used in the offering period, including regularly released forward-looking information. Furthermore, the antifraud protections under section 17(a) of the Securities Act and section 10(b) of the Exchange Act would attach to any communication that constitutes an offer or is in connection with the sale of a security, respectively, regardless of whether it was made during the offering period. Thus, communications made prior to filing (or prior to thirty days before filing for Form A registrants) would no longer technically constitute "offers" under the Aircraft Carrier's pre-filing period proposals. Since the Reform envisions a financial developments regarding the issuer, dividend notices, information in Exchange Act reports, and responses to unsolicited inquiries from stockholders, analysts, or the press, but do not include information about the offering itself. See id. § VII(A)(1)(c)(ii)(A) at 81,522. Regularly released forward-looking information must be usually released in the ordinary course of business, and includes such items as financial projections, statements of management's plans and objectives, and statements about future economic performance. See id. § VII(A)(1)(c)(ii)(B), at 81,522.

122. See id. § VII(A)(2), at 81,523.
123. See id. § VII(A)(2), at 81,524. "Free writings" generally refer to sales literature that is prohibited during the pre-filing and waiting periods.
124. See id. § V(C), at 81,499-502. Section 11(a) of the Securities Act attaches civil liability to issuers, underwriters, and accountants for "any part of the registration statement, when such part [becomes] effective, contain[ing] an untrue statement of a material fact or omit[ting] to state a material fact required to be stated therein or necessary to make the statement therein not misleading." 15 U.S.C.A. § 77k (West 1997).
125. See Reform Release, supra note 104, § V(C)(2)(b), at 81,501. Section 12(a)(2) of the Securities Act provides civil liability against "any person who offers or sells a security... which includes an untrue statement of a material fact or omits to state a material fact necessary in order to make the statements, in light of the circumstances under which they were made, not misleading..." 15 U.S.C.A. § 77q(a)(1) (West 1997).
126. See Reform Release, supra note 104, § V(C)(2)(c), at 81,501. Section 17(a) of the Securities Act makes it unlawful for "any person in the offer or sale of any securities... to employ any devise, scheme, or artifice to defraud..." 15 U.S.C.A. § 77t(a)(1) (West 1997). Section 10(b) of the Exchange Act makes it unlawful "to use or employ, in connection with the
shift away from pre-effective review and toward further reliance by investors on incorporated Exchange Act filings (now readily available to most investors via EDGAR on the SEC’s web site), the Aircraft Carrier Release aims to improve the accuracy and completeness of these filings by requiring signatories of Exchange Act reports and registration statements to certify that the report or statement contains no material misstatement or omission. The Aircraft Carrier Release would also expand the group of persons required to sign several forms (including the 10-Q) to include the “principal executive officers of the registrant and a majority of the board of directors of the registrant.”

The Aircraft Carrier Release also aims to strengthen investor protection by re-focusing the prospectus delivery requirements from prospectus delivery at or before final confirmation of sale to prospectus delivery before the point in time when an investor has already made his investment decision. Section 5(b)(2) of the Securities Act requires issuers to send investors a final prospectus no later than the time of sale. Though the SEC has adopted rules to give issuers an incentive to send a preliminary prospectus to investors earlier in the process, doing so is not required except under very limited circumstances. The Aircraft Carrier Release would provide an exemption to the prospectus delivery requirement. As a condition of the exemption, Form B registrants would be required to deliver either a term sheet or a preliminary prospectus containing transactional information before the investment decision is made, while Form A registrants would be required to deliver a preliminary prospectus three days before the security is priced or, in the case of an initial public offering, seven days before pricing. Issuers would also have to inform investors by the time they have received

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127. EDGAR stands for the Electronic Data Gathering, Analysis, and Retrieval system. EDGAR performs automated collection, validation, and indexing of submissions by companies required to file forms with the SEC and makes such information publicly available via the SEC’s web site. See EDGAR Database of Corporate Information (last modified Feb. 22, 2000) <www.sec.gov/edgarhp.htm>.

128. Reform Release, supra note 104, § XI(C), at 81,566.


130. See, e.g., Securities Act Rules, 17 C.F.R. § 230.460 (1999) (allowing the SEC, when ruling upon requests for acceleration of effectiveness of a registration, to take into account whether the preliminary prospectus has been adequately distributed); Exchange Act Rules, 17 C.F.R. § 240.15c2-8 (1999) (requiring brokers and dealers to deliver a preliminary prospectus to investors 48 hours prior to confirmation of sale in the case of initial public offerings).

131. See Reform Release, supra note 104, § VIII(C)(3), at 81,536.

132. See id. § VIII(C)(4)(a)–(b), at 81,538.
confirmations of sale where they can acquire a final prospectus. Investment banks have criticized the term sheet proposal, arguing that it will significantly slow down offerings by large issuers who currently can use the shelf registration system to offer securities in a matter of hours.

B. Effect of the Aircraft Carrier Release on Internet Securities Offerings

The rise of information technology was clearly an important factor in producing the Aircraft Carrier Release. Indeed, the SEC noted in the Release that, "[t]echnological innovations that permit instantaneous communications are a driving force behind this decade's securities market." In addition, the SEC cites the increasing ability of investors to access information from corporate web sites and from company filings made publicly available on the SEC's own web site. To encourage investors to make use of these resources, the Aircraft Carrier Release requires issuers to provide their web site address and an electronic mail contact on the cover page of registration statements filed under the Securities Act.

Arguably the most important part of the Aircraft Carrier Release, in terms of its impact on the Internet, is the proposed removal of restrictions on communications during the pre-filing and waiting periods. One major impact of these changes relates to electronic roadshows. By eliminating the restriction that communications during the waiting period be limited to the preliminary prospectus, the Aircraft Carrier Release removes the need for electronic roadshow companies to receive no-action letter assurance that their individual system will not be deemed to violate section 5(b)(1) of the Securities Act. In addition, the Aircraft Carrier Release would allow

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133. See id. § VIII(C)(3)(a), at 81,536.
134. Shelf-registration allows securities to be offered or sold on a delayed or continuous basis. Specifically, Securities Act Rule 415 allows large issuers to file for offerings of equity securities that they plan to offer within two years of the effective date of the registration statement. See Securities Act Rules, 17 C.F.R. § 230.415 (1999).
135. See Charles Sisk, Bankers Fret SEC Overhaul May Slow Down Offering Process, CORP. FINANCING. Wk., Feb. 22, 1999, at 1 (noting the claim by counsel for the Securities Industry Association that the term sheet requirement could delay shelf registration for days while issuers' and underwriters' lawyers examine term sheets for potential liabilities).
137. See id. § V(A)(1)(a)(i), at 81,476.
138. See id. § VII(C), at 81,526.
139. See New Rules Would End Road Show No-Action Requests, FIN. NET NEWS, Nov. 23, 1998 at 6; supra Part I.C.
companies conducting electronic roadshows to communicate not only with institutional investors and analysts, but to retail investors as well.\textsuperscript{140} The SEC seems to have placed a priority on broadening the audience for roadshows because of its understandable concern that roadshow presentations promote selective and unfair disclosure to a privileged few.\textsuperscript{141} Though some have argued that selective disclosure does not hurt the investing public because information given to institutional or other large investors is quickly incorporated into the price of securities through their purchases and sales, the SEC at least believes that the retail market has been playing an important role in setting prices as well, especially with high technology stocks.\textsuperscript{142} Finally, the proposal would allow issuers to accompany the roadshow presentation with written material (and make them more likely to allow investors to keep such material), thus increasing the informational value of such presentations to investors.\textsuperscript{143}

Though the proposed reforms should generally increase issuers' ability to use electronic roadshows, the requirement that all free writing be filed with the SEC may dampen issuers' enthusiasm. Even outside the context of the Internet, the proposed filing requirement has produced widespread criticism from securities lawyers who have argued that it would be extremely burdensome to file all free writing material and that the increased liability risks associated with filing would ironically result in a greater shift from written to oral communications than has occurred under the present system.\textsuperscript{144} Such

\textsuperscript{140} See Reform Release, \textit{supra} note 104, § VII(C), at 81,525 ("[I]ssuers and underwriters could use the Internet and other electronic media to, among other things, conduct electronic roadshows to institutional and retail investors without the use of password protection . . . ."); \textit{New Rules Would End Road Show No-Action Requests, supra} note 139 at 6 (noting that limits on who accessed electronic roadshows would no longer be relevant under the Aircraft Carrier Reform proposal).

\textsuperscript{141} See Reform Release, \textit{supra} note 104, § VII(A)(2), at 81,523 ("Issuers and their agents are known to deliberately provide some information during the waiting period only orally, and also limit the audience to avoid those communications being considered broadcasted. Perhaps the best example of how the current regulatory structure negatively affects investors is the 'road show' structure.").

\textsuperscript{142} See Isaac C. Hunt, Jr., Speech by SEC Commissioner: Navigating the Sea of Communications at the Practicing Law Institute's SEC Speaks (Feb. 26, 1999), available in 1999 WL 106714 (S.E.C.), at *3 (arguing that the Aircraft Carrier proposal will bring greater fairness to the market by attacking the "insidious problem of selective disclosure").


\textsuperscript{144} See, \textit{e.g.}, Charles Sisk, \textit{Street Ready to Take Shots at SEC Flagship}, \textit{Corp. Financing Wk.}, Nov. 30, 1998, at 8 ("Most security lawyers say it would be impossible for companies to file all their communications with the SEC, as it would be too difficult to record and track everything."); "\textit{Aircraft Carrier} Sprouts Leaks, supra" note 105 (noting that "companies could just end up concentrating more on oral communications to reduce filings, and
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action is especially likely in the context of electronic communications because the Aircraft Carrier Release does not clarify the complicated question of what a "writing" is for the purposes of the filing requirement. Issuers worried about section 12(a)(2) liability for free writings may, therefore, steer wide and clear of anything that could remotely be deemed a writing, making less use of Internet communications than they might otherwise do. Ironically, the SEC seems to acknowledge the difficulty of truly distinguishing oral and written communications in the electronic age by its deregulatory policy toward pre-filing and waiting period communications, but at the same time it is implementing a filing requirement that applies to free writings. Electronic roadshows are but one example of the way in which technology has undermined the difference between oral and written communications; the problem can only become more pronounced with the increasing use of multimedia. If the SEC requires issuers to file multimedia presentations, an additional problem is how exactly this should be done given that even the new EDGAR II system will be unable to accommodate multimedia.

Beyond roadshows, the SEC also hopes that the deregulation of communication restrictions during the waiting period will generally allow issuers to make creative use of the Internet and other media technologies to communicate and deliver information to potential investors. The Aircraft Carrier Release notes in particular that issuers would be able to use electronic mail to answer investors' questions about the company and its offering, to engage in "chat room" discussions with investors, and to post messages on bulletin boards about its offering. Again, it is not always clear whether and how these and other materials would be filed with the SEC. For example, would all participants' comments in a chat room discussion need to be filed as free writings, or just the contributions of the company? Could a transcript of a streaming video presentation or a video conference,

thus liability.


146. See Unger, supra note 105, at 33 ("Issuers' growing use of multimedia in traditional written documents and digital information in voice applications has made it difficult for counsel and the Commission staff to determine what is a 'writing' under the Securities Act of 1933.... The problem will multiply as text and multimedia become more intertwined.").

147. See Reform Release, supra note 104, § VII(B), at 81,525; Unger, supra note 105, at 34.

148. See Reform Release, supra note 104, § VII(C), at 81,525.
neither of which can be recorded, ever provide a fair and accurate representation for other investors? Furthermore, it is not always clear whether filing such information would be of any help to investors. Would, for example, voluminous electronic mail correspondence between a company and potential investors be of any help to other investors?  

Another popular use of the Internet that is commonly used by companies to communicate with their investors is corporate web sites. The easing of restrictions on communications is designed to allay at least some concerns regarding liability associated with material posted on or hyperlinked to issuers' web sites. By allowing offers during the pre-filing period, the Aircraft Carrier Release would allow issuers to advertise or provide information about an upcoming offering on their web sites. Thus, issuers would no longer have to worry that something posted on their web site could be interpreted after the fact as a solicitation for an offering. Form A registrants, however, would need to remove any materials not covered by the proposed safe harbors (e.g., "factual business information" and "regularly released forward-looking information") thirty days before filing. By allowing free writings during the waiting period, the Aircraft Carrier Release allows companies conducting an offering of securities to post information relating to the offering on their web site, and to hyperlink to additional relevant information.

Though the easing of restrictions on communications is a positive step, the Aircraft Carrier Release will by no means end concerns over liability stemming from corporate web sites. First, liability is more likely to stem from postings or hyperlinked material being deemed violations of Securities Act section 12(a)(2) or the antifraud provisions than a violation of the section 5 prohibition on communications during the waiting period. Second, the Aircraft Carrier Release may create new difficulties relating to hyperlinks. One reason is the requirement that all free writing material be filed

149. See Unger, supra note 105, at 34.
150. See Allyson Vaughan, The Offering Quite Period, FIN. NET NEWS, Oct. 19, 1998, at 8 (noting that "[i]f a firm is communicating with the public during the period of the offering or before the offering, firms must ensure communications are not construed as advertising.").
151. Reform Release, supra note 104, § VII(A)((c)(i), at 81,521.
152. Cf. Boris Feldman, Investor Relations on the Internet: A Securities Disclosure Perspective, OFF-LINE, Winter 1996, at 1, 2, 4 (warning that plaintiffs' lawyers will look on company web sites for forward looking statements that did not come true and for hyperlinks to positive analyst reviews).
with the SEC. Consistency with the “envelope theory” would mean that an issuer would be required to file third party materials if its website has a hyperlink to such material. If the SEC were to consider imposing such an obligation, it would also have to determine whether such an obligation would be affected by the type of link between the sites, which could vary from a framed link (in which the material from one site is framed by the prior site) to a hyperlink with a prominent exit notice. Hyperlinks also risk running afoul of the requirement that all free writings be accompanied by language instructing investors to read the disclosure documents filed with the SEC. In theory, a company could be liable for failing to provide such language if another site was hyperlinked deep into its website so as to bypass any cautionary language. Practically, it may also be difficult for a company to file a description of third party free writing material when the company has no control over the content of the third party’s website, which could be changed at any time. Such risks may mean that issuers will make less use of Internet websites both to avoid the costs of monitoring numerous web pages and to reduce the risk of liability for filed free writings under section 12(a)(2) of the Securities Act.

The Aircraft Carrier Release’s prospectus delivery proposals may also affect Internet usage. However, the new approach should merely shift, but not reduce, the difficulties involved in electronic dissemination of required information. On the one hand, the elimination of the requirement that a final prospectus be delivered before sale makes the many difficulties involved in meeting the notice, access, and delivery criteria irrelevant. The Aircraft Carrier Release requires only that an issuer inform investors of where they can obtain the information that constitutes the final prospectus free of charge. A note sent along with the term sheet (in the case of Form B issuers) or presumably with either the preliminary prospectus or even the confirmation letter (in the case of Form A issuers) telling investors that the final prospectus is available on the issuer’s and/or the SEC’s website would be sufficient to meet this requirement. On the other hand, the requirement that investors be provided with a

153. See supra note 77 and accompanying text.
154. See Unger, supra note 105, at 33.
157. See Reform Release, supra note 104, § VIII(C)(3)(a), at 81,536.
158. See id. § VIII(C)(3)(a) n.395.
term sheet or preliminary prospectus before the investment decision is made would seem to raise all the notice, access, and delivery concerns that currently apply to the final prospectus. Furthermore, current Exchange Act Rule 15c2-8, which mandates that broker-dealers deliver a final prospectus to investors forty-eight hours before sale in the case of an initial public offering, notably does not apply to issuers.159 Therefore, in a direct public offering conducted over the Internet (which by definition would not utilize a broker-dealer), the prospectus need only be delivered upon sale, creating a unique benefit to Internet-based direct public offerings in the current system.160 However, the Aircraft Carrier Release Provisions involving the term sheet and preliminary prospectus explicitly apply to issuers as well as broker-dealers, thereby creating the same delivery requirements for direct public offerings and all other offerings.

III. CONCLUSION

The combination of substantial cost savings and an unprecedented ability to reach millions of investors means that issuers have strong incentives to utilize the Internet to raise capital. Fear of liability, however, can easily stifle innovation in this area. Though the SEC has so-far embraced new technologies, such as EDGAR, the current regulatory regime still assumes a paper-based world. Where it does not, the laws draw paper-based analogies: the envelope theory; the requirement of substantial equivalence between electronic and paper delivery; and the proposal that free writings be filed. With the increasing use and complexity of multimedia communications, the SEC will continually need to revisit its assumptions. The Aircraft Carrier Release reveals the SEC’s ability to do so. However, while the current approach to reform does aid issuers who use new technologies in important ways, this paper has also shown that some serious pitfalls remain for those involved in securities offerings conducted over the Internet.

The SEC could further promote the use of the Internet in securities offerings in two specific ways. First, the SEC should provide official guidance, either in the form of a release or regulations, to issuers conducting securities offerings over the Internet that are exempt from the registration requirements. Companies wishing to raise small sums over the Internet, or services linking such issuers with investors, should no longer have to rely on a string of

160. See Reform Release, supra note 104, § VIII(C)(1), at 81,535.
no-action letters to guide their actions. Indeed, the president of IPONet has complained that most companies have refused to use his service due to fear of liability, despite the fact that IPONet itself was granted a no-action letter.\textsuperscript{161}

Second, the SEC should eliminate the proposed requirement that free writings disseminated during the pre-filing or waiting periods be filed with the SEC. This requirement could undermine many of the provisions, especially those relating to pre-filing and waiting period communications, that would otherwise promote the use of the Internet. The requirement is also unnecessary: when information is made publicly available on the Internet (for example by posting it on a company’s own web site), there is no need for the same information to be filed with the SEC, who would merely post this information on its own web site. This is not to say that no investor protection is needed, but perhaps there are other possibilities, such as a requirement that such material remain on an issuer’s web site for the duration of an offering. In addition, the antifraud provisions would still apply to all such material, whether filed or not. Thus, eliminating the filing requirement could potentially go a long way toward helping to integrate the Internet and its many possibilities into the securities offering process.

\textsuperscript{161} See Reinbach, \textit{supra} note 3, at 40. Leo Feldman, the company’s president, explained why 20 companies to whom he had talked about participating in IPOs turned him down.

Their biggest fears are that something might be released by e-mails or something else that would prompt the Securities and Exchange Commission (SEC) to step in and say they were gun-jumping or something... It’s been like pulling teeth.... Everybody is afraid. The underwriter’s counsel are afraid, even though I have a No Action letter from the SEC [stating that it will not interfere with IPO.Net’s Web IPOs]; they don’t think I can do this. When you talk to counsel of the issuer, you run into trouble, and [the same] when you start talking to counsel of the broker-dealer. Nobody wants to opine to the fact that this is legal.

\textit{Id.}