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COVID-19 RESOURCES

COVID-19: Equity Fundraising Options for Listed Companies in Asia

15 April 2020

With the COVID-19 pandemic continuing to overwhelm economies, a number of listed companies globally have already recapitalized through equity fundraising in the capital markets. New equity has helped these companies shore up their balance sheets and obtain liquidity. This *Alert* discusses equity fundraising options for listed companies in Asia and complements our prior *Alert* that discussed options for Asian companies to manage their outstanding bond liabilities.

Rights Offers, Follow-On Offers and Private Placements: Choosing an Offering Structure

Listed companies seeking to raise equity must decide between offering their new shares publicly or privately. Public offerings can be made either pro rata to all existing shareholders by issuing them rights to purchase new shares (rights offer) or by selling new shares to retail and institutional investors (follow-on offering). Private placements are generally made only to institutional investors, who can be either new or existing shareholders. The choice of structure depends on several factors, including (i) whether shareholders are entitled to preemptive rights, (ii) whether the company wants certainty of funding and whether substantial shareholders can help provide that and (iii) whether shareholder and regulatory approvals are required.

Preemptive Rights

The threshold question for companies to consider is whether existing shareholders are entitled to preemptive rights to participate in any new sales of shares. Preemptive rights can exist under corporate or securities law in the jurisdiction of incorporation and (if different) the jurisdiction in which the shares trade, as well as the rules of the stock exchange on which the shares trade and the company's constitutional documents. If preemptive rights exist, the only options are to undertake a rights offer or to ask shareholders to waive their preemptive rights.

Substantial Shareholders and Certainty of Funds

Where preemptive rights do not exist, the presence of a substantial shareholder, such as a founder, financial sponsor or parent company, often drives the choice of offer structure. Where a substantial shareholder is seeking to inject equity, a rights offer is generally necessary to avoid minority oppression. Participation by substantial shareholders significantly reduces the amount of equity needed from public investors, and substantial shareholders often commit to purchase any shares that remain unsubscribed by other investors (rump shares), providing certainty of funds.

If substantial shareholders do not exist or are not willing to invest, but companies still want certainty of funds, they can appoint an underwriter (or "backstop purchaser" in case of a rights offer), typically an investment bank. Underwriters agree to purchase any unsubscribed shares in the offering. Alternatively, for companies that do not need certainty of funds, they can appoint a placement agent, again typically an investment bank. Placement agents act on a best-efforts basis to find buyers for the shares being offered.

Underwriters and placement agents can be used in connection with any of the offer structures and are paid fees for their participation. As underwriters take on undersubscription risk, whereas placement agents do not, underwriting fees tend to be significantly higher than placement agent fees.

Approval and Documentation Requirements

The approval and documentation process can vary substantially across offer types and jurisdictions. Seeking shareholder or regulatory approval, and the associated documentation needed for those, can significantly slow a transaction's speed to market. Companies with an urgent need for capital may need to choose a structure that does not require approvals.

In terms of shareholders' approval, companies commonly have a general mandate from shareholders to undertake small equity raises without specific approval for the transaction in question. Most jurisdictions, either under law or stock exchange rules, place limits on the scope of the general mandate. Private placements and follow-on offers tend to be strictly controlled in order to protect against undue dilution to existing shareholders. These controls typically place limits on the transaction's size and/or discount to market price. Rights offers do not dilute shareholders who exercise their rights, and hence tend to allow much larger offer sizes and in many cases have no limit whatsoever on discounts[1] before requiring specific shareholder approval.

In terms of regulatory approval, some jurisdictions require approval where shares are offered to retail investors, as is the case in rights offers and follow-on offers. In such cases, a prospectus must be registered with the local securities regulators prior to the offer, which is time consuming. As private placements are generally made only to institutional and sophisticated investors, they generally do not require regulatory approval, although some jurisdictions still require an offering memorandum to be sent to investors.

Given that the legal requirements differ in every jurisdiction, companies should consult their local legal counsel. Notwithstanding the legal requirements, it can still be prudent to prepare, and investment banks on a transaction may require, an offering memorandum to ensure that offerees have all material information about the company. If a company is accessing the international markets for the first time, does not publish its ongoing disclosure in English or is in a jurisdiction where the

[1]The maximum discount can also depend on whether the rights are transferable or non-transferable (see Transferable and Nontransferable Rights below). This is the case for Singapore-listed companies, for whom transferable rights (called renounceable rights issues in Singapore) have no limit on the discount to market price, whereas non-transferable rights (called preferential offerings in Singapore) are subject to a maximum discount of 10 percent.

ongoing disclosure requirements are not extensive, international investors will likely want to receive an offering memorandum.

Transferable and Nontransferable Rights

Rights offers can involve transferable or nontransferable rights, depending on local law. Where rights are transferable, shareholders can choose either to exercise them or to sell them on the stock exchange. Transferable rights provide shareholders who do not want to exercise their rights with a way to earn a profit on the rights, helping to offset potential dilution for shareholders who do not exercise their rights.

Foreign Registration Requirements

Companies seeking to raise equity from international investors also need to consider foreign registration requirements. Most countries strictly regulate the offer and sale of securities to their residents. While a detailed survey of the registration requirements of every jurisdiction is beyond the scope of this *Alert*, as a general matter most countries provide exemptions for offers and sales that are made only to defined categories of sophisticated or institutional investors, or those made only to a limited number of investors. These exemptions typically place restrictions on the way the offering is communicated to investors, such as by preventing widespread advertisement. Some countries also require pre-trade or post-trade filings with regulators.

Follow-On Offerings and Private Placements

In the case of follow-on offerings and private placements, complying with foreign registration requirements is not generally burdensome. Companies have the flexibility to choose their target investor base and can limit foreign investors to sophisticated institutions. They also can limit offerings to major financial centers, perhaps with a small number of additional jurisdictions relevant to the company in question, such as where they have significant operations. Companies are therefore able to reasonably limit the amount of foreign legal advice they need while maintaining access to a large pool of investors.

Rights Offers

For rights offers, complying with foreign registration requirements can prove daunting. Rights offers include all existing shareholders and it can be difficult or impossible for a listed company to determine where its shareholders are, as shares trade freely on a stock exchange and many are held through nominees or custodians. Even if the location and identity of foreign shareholders can be determined, there is no guarantee that exemptions will be available to allow offering shares to all of them, as they may not meet any sophistication or number requirements applicable under foreign law.

For these reasons, rights offers often specifically exclude participation by shareholders who are in jurisdictions in which it would be unlawful to offer or sell them securities, or in which a regulatory approval would be required. This option is not available for every company, however, as the company's constitutional documents or applicable corporate or securities laws may require the rights offer to be available to *all* shareholders regardless of their location. Some countries allow exceptions to the all-shareholders requirement where it would be unduly burdensome or expensive to include particular shareholders, but that is not always the case. Companies are advised to consult with their local counsel on these matters.

In order to discourage the practice of broadly excluding groups of shareholders, some countries, such as the United States, have created specific exemptions through which foreign companies can make rights offerings available to their residents (see Rule 801 Rights Offers, below).

U.S. Federal Securities Laws

The U.S. Securities Act of 1933, as amended (Securities Act), requires that any transaction involving the offer or sale of a security be registered with the Securities and Exchange Commission (SEC), or meet an applicable exemption from registration. The terms "offer" and "sale" apply to any sale or disposition of a security, or an offer to dispose of or solicitation of an offer to buy a security, "for value."

For follow-on offers and private placements, the shares are sold to investors for cash, which is something of "value". For rights offers, U.S. law distinguishes between the issuance of rights by a company and the exercise of those rights by holders. As rights are issued to shareholders without consideration, they do not need to be registered. However, the exercise of rights requires cash payment, which brings the exercise of rights within the registration requirements of the Securities Act.

The registration requirements of the Securities Act therefore apply regardless of offer structure. Three registration exemptions that are frequently used by foreign listed companies are: (i) Regulation S under the Securities Act (Regulation S), (ii) Rule 144A under the Securities Act (Rule 144A), and (iii) Section 4(a)(2) of the Securities Act (Section 4(a)(2)). A fourth exemption, Rule 801 under the Securities Act (Rule 801), applies specifically to rights offers, though is not widely used by Asian issuers.

Regulation S Sales Outside the U.S.

Regulation S exempts all offers and sales that occur outside the U.S. and defines conditions in which an offer will be deemed to occur outside the U.S. All Regulation S transactions have two fundamental requirements: (i) that the offer be made in an "offshore transaction"[2] and (ii) that no "directed selling efforts"[3] can be made in the U.S. Regulation S imposes additional requirements on companies that have a stronger nexus to the U.S., such as those for which there is a "substantial U.S. market

[2] An offer or sale of securities by an issuer is defined to be made in an "offshore transaction" if either (i) at the time the buy order is originated, the buyer is outside the U.S., or the seller and any person acting on its behalf reasonably believe that the buyer is outside the U.S., or (ii) the transaction is executed in, on or through a physical trading floor of an established foreign securities exchange that is located outside the U.S.

[3] "Directed selling efforts" means any activity undertaken for the purpose of, or that could reasonably be expected to have the effect of, conditioning the market in the U.S. for any of the securities being offered in reliance on Regulation S. The prohibition on directed selling efforts applies to the issuer, a distributor of the securities, their respective affiliates, or any person acting on behalf of any of the foregoing.

interest"[4] in the class of shares being offered or sold or for those that are not a "foreign issuer"[5]. For companies that do not implicate the additional requirements, Regulation S provides an easy and effective way of avoiding the U.S. registration requirements by excluding U.S. investors from the offering. However, U.S. investors may be necessary to include in order to realize the desired pricing or size for the offering, and a decision to exclude them should only be made upon consultation with the financial adviser appointed for the transaction.

U.S. Private Placements Under Rule 144A and Section 4(a)(2)

Rule 144A exempts offers and sales from registration so long as the shares are sold only to "qualified institutional buyers" (QIBs)[6], or persons that the seller and any person acting on their behalf reasonably believe is a qualified institutional buyer. In addition, the seller must take "reasonable steps" to ensure that the buyer is aware the seller is relying on Rule 144A, the shares cannot be of the same class as securities listed on a U.S. national securities exchange, and the buyer must have a right to receive "reasonably current" information about the company and its financial statements. As a technical matter, Rule 144A is only available for *resales* of securities, meaning that is not available for direct sales by an issuer to its investors. However, transactions can be structured to include an investment bank as an intermediary, whereby the issuer sells the shares to the investment bank who then on-sells the shares to the investors. This structure is commonly used where there is no stamp duty or transfer tax on the sale of shares, such as the in the U.S., but not in those countries where there are such taxes. If a country has stamp duty or transfer tax on the sale of shares, the sales are generally made pursuant to Section 4(a)(2) of the Securities Act.

Section 4(a)(2) of the Securities Act exempts from registration any transaction by an issuer not involving any public offering. The Securities Act does not define the conditions that must be met to satisfy Section 4(a)(2), and U.S. case law on this point has left the analysis highly fact specific. Accordingly, Section 4(a)(2) offers are often structured to mirror as closely as possible Rule 144A offerings. In particular, the most important practice is to limit the investor pool in the U.S. to QIBs and to limit U.S. marketing activities. It is possible to expand Section 4(a)(2) offerings beyond QIBs to include "accredited investors" in compliance with Regulation D, and in certain markets this is not particularly unusual. However, offerings by issuers from Asia generally limit U.S. sales only to QIBs on the basis that it is not commercially necessary to target a wider audience. Where accredited

[4] A "substantial U.S. market interest" with respect to an issuer's equity securities exists if either (i) the securities exchanges and inter-dealer quotation systems in the U.S. in the aggregate constituted the single largest market for such class of securities in the shorter of the issuer's prior fiscal year or the period since the issuer's incorporation, or (ii) 20 percent or more of all trading in such class of securities took place in, on or through the facilities of securities exchanges and inter-dealer quotation systems in the U.S. and less than 55 percent of such trading took place in, on or through the facilities of securities markets of a single foreign country in the shorter of the issuer's prior fiscal year or the period since the issuer's incorporation. Companies with ADRs listed in the U.S. should note that ADRs are treated as the same class of securities as the shares underlying the ADRs.

[5] A company is a "foreign private issuer" if it is incorporated or organized under the laws of a non-U.S. jurisdiction, unless (i) more than 50 percent of its outstanding votes securities are directly or indirectly owned of record by U.S. residents, and (ii) (a) a majority of its executive officers or directors are U.S. citizens or residents, (b) more than 50 percent of its assets are located in the U.S. or (c) its business is administered principally in the U.S.

[6] A "qualified institutional buyer" is an entity that owns and invests on a discretionary basis at least US$100 million in securities of issuers that are not affiliated with it, and that fall within one of a long-list of types of legal entities, such as insurance companies, investment advisers, benefits plans and certain trusts and other entities

investors are included, they usually have close, preexisting relationships with the company, such as being one of its directors or executive officers.

Rule 801 Rights Offers

For companies that are prohibited from excluding particular groups of shareholders from a rights offer, a Rule 801 offering is likely to be the only available exemption from U.S. registration. Rule 801 is available for foreign private issuers[7] whose U.S. shareholders hold no more than 10 percent of the class of shares being offered, provided that certain conditions are met (as described below).

Rule 801 requires companies to attempt to "look through" nominees, custodians and other intermediaries to determine beneficial ownership. Companies must make a reasonable inquiry of intermediaries in the U.S., the company's jurisdiction of incorporation and the jurisdiction in which the shares are primarily traded to attempt to determine the level of beneficial ownership by U.S. residents. If, after reasonable inquiry, they are unable to determine the amount represented by U.S. residents, they may assume that the customers reside in the jurisdiction in which the intermediary has its principal place of business. While shareholder analyses are possible, they add cost, complexity and time to the proposed offering. Therefore, many companies use Rule 801 only as a last resort.

Rule 801 has the following additional conditions:

1. The company must allow U.S. shareholders to participate on terms at least as favorable to those offered to other shareholders (however, companies need not extend the rights offering to U.S. states or jurisdictions that require registration or qualification).

2. If the company publishes an informational document in connection with the rights offer, it must furnish a copy, in English, to the SEC on Form CB. The company must disseminate the informational document to U.S. holders on a comparable basis to that provided to shareholders in its home jurisdiction and it must publish the information in the U.S. in a manner reasonably calculated to inform U.S. shareholders of the offer. Together with the Form CB, the company must file a Form F-X, through which it appoints an agent for service of process in the U.S.

3. The shares in the rights offer must be of the same class as the shares held by U.S. holders directly or through ADRs.

4. The company must prohibit transfer of the rights by U.S. holders except for transfers made outside the U.S. in accordance with Regulation S.

5. Any informational document sent to U.S. holders must include a prominent legend in a format prescribed by the SEC (or its equivalent in clear, plain language).

While Form CB is "furnished" rather than "filed" with the SEC and is, therefore, exempt from certain antifraud provisions in the U.S. federal securities laws, the overarching antifraud provisions under Rule 10b-5 still apply to Form CB submissions (see U.S. Antifraud Liability, below, for details).

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[7] See footnote 4 above for the definition of a "foreign private issuer".

If a company determines that U.S. holders exceed the 10 percent limit or if it is unable to meet any of the other requirements of Rule 801, the only remaining options are to register the rights offer with the SEC (which subjects the company to the reporting framework applicable to U.S. public companies), find a way under local law that allows exclusion of U.S. shareholders, or cancel the rights offer.

State "Blue Sky" Registration Requirements

If a rights offering will be conducted in the U.S. pursuant to Rule 801, it is still necessary to ensure compliance with or an exemption from the securities laws of the U.S. states (commonly called "blue sky" laws) where shareholders reside. Although Rule 801 does not require companies to extend a rights offering to shareholders in those U.S. states or jurisdictions that require registration or qualification, this may not be possible if the local laws of the company prevent such disparate treatment of shareholders. In this situation, blue sky law filings may be required, which we can arrange.

U.S. Antifraud Liability

Regardless of the offer structure chosen, U.S. law prohibits fraud, manipulative or deceptive practices and misleading statements or omissions of material fact in connection with the purchase or sale of a security. This prohibition extends even to offers and sales that are exempt from Securities Act registration, such as those relying on Rule 144A, Section 4(a)(2) or Rule 801. Accordingly, foreign-listed companies seeking equity fundraising from investors in the U.S. should either prepare an offering memorandum in connection with the transaction or be comfortable that their existing public disclosure in their home market is up to date, robust and includes the type and scope of information generally required under U.S. securities laws.

For Further Information

If you have any questions about this *Alert*, please contact Jamie A. Benson, Jonathan E. Crandall, Gerard A. Hekker, any of the Asia- or U.S.-based attorneys in our Capital Markets Group or the attorney in the firm with whom you are regularly in contact.

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About our U.S. Capital Markets Practice in Asia

We are experienced representing issuers and underwriters on Section 4(a)(2), Rule 144A, Rule 801 and Regulation S global offerings, and U.S.-registered offerings.

Our three U.S. capital markets partners in Singapore – Jamie Benson, Jonathan Crandall and Gerard Hekker – combine broad global training with deep Asian experience, having advised on over 175 debt and equity capital markets transactions across Singapore, the United States, the United Kingdom, Australia, Hong Kong, India, Indonesia, Malaysia, Myanmar, New Zealand, the Philippines, Thailand and Vietnam, with over US$50 billion raised in aggregate.

We offer clients an unrivalled value proposition and distinguish our services from our competitors with the high level of our partners' involvement in matters. Our partners engage in drafting documentation and lead the daily interaction and communication. We believe that this differentiates our value proposition by giving the best possible advice on the spot, thereby saving time, increasing efficiency and supporting our adherence to budget.

COVID-19 Strategy Teams

Duane Morris has created a COVID-19 Strategy Team to help organizations plan, respond to and address this fast-moving situation. Contact your Duane Morris attorney for more information. Prior *Alerts* on the topic are available on the team's webpage.

Duane Morris & Selvam's Singapore office has also created a COVID-19 Strategy Team to help organizations plan, respond to and address this fast-moving situation. Contact your Duane Morris & Selvam attorney for more information. Prior *Alerts* on the topic are available on the team's webpage.