



PIPEs TRANSACTIONS

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What is a PIPE?

- A PIPE is a Private Investment in Public Equity – a private placement by a publicly-traded company to raise additional capital, typically for growth, to fund acquisitions or to repay debt.
- PIPEs are often used by smaller public companies as their primary financing vehicle, and by larger companies to fund specific transactions.
- Investors generally consist of a small group of institutional investors such as hedge funds, and/or accredited individual investors.
- In a PIPE financing, the company may issue common stock, convertible preferred stock, convertible debt, or a combination of these or other securities.
- Investors in PIPE transactions often receive warrants to purchase additional shares of common stock.
- Immediately following the closing of the PIPE transaction, the company typically files a registration statement with the SEC to enable the PIPE investors to re-sell the shares of common stock (or shares issuable upon conversion of convertible securities) purchased in the PIPE.

Advantages and Disadvantages of PIPE Transactions

■ Advantages:

- Speed to Market: Most PIPE transactions are completed within two to three weeks of beginning the process. Secondary public offerings can take several months.
- Confidentiality: No disclosure is required until the investors sign a definitive agreement with the company. In contrast, a secondary offering requires full disclosure early in the process.
- Less volatility in the stock price prior to closing reduces potential impact on pricing.
- No impact on public market of a failed transaction.
- Reduced expenses (placement agent, legal, accounting, printing).
- No SEC review of documents until post-closing registration statement is filed.
- Limited documentation.
- Limited due diligence by investors and placement agent.
- Infrequent road shows.

Advantages and Disadvantages of PIPE Transactions

■ Disadvantages:

- Significant discounts to current trading price.
- Warrants required as “sweetener” to investors.
- Penalties (typically 1-2% per month) for failure to timely register securities for resale after the PIPE closing (typically 10-30 days to register, 90-120 days to become effective).
- Frequently results in substantial dilution to current shareholders.
- May lead to concentration of ownership.
- Company typically required to maintain effectiveness of registration statement for up to two years.
- Risk of insider trading by potential PIPE investors.
- Risk of short selling leading to downward pressure in stock price.

Current Issues in PIPE Transactions

- Rule 415 – Background
 - Rule 415 permits resales of privately-placed securities by investors in registered secondary offerings at market prices.
 - Companies may use S-3 short-form registration statements for secondary offerings if they:
 - Have been public for at least one year;
 - are current in their SEC filings; and
 - are traded on the NYSE, AMEX or NASDAQ.
 - Beginning in 2006, the SEC began questioning whether resales under Rule 415 by PIPE investors were actually primary offerings of stock by the company

Current Issues in PIPE Transactions

- Rule 415 - Current SEC Guidance

- SEC will question primary vs. secondary offering if shares registered exceed 33% of the company's pre-PIPE public float (shares held by non-affiliates).
- Determined through the comment letter process on registration statements on a case-by-case basis. Factors considered include:
 - Size of transaction
 - Concentration of ownership
 - Other indicia of control (e.g. board seats)
 - Number and identity of investors
 - Discount to current trading price.

Current Issues in PIPE Transactions

- Rule 415 - Current SEC Guidance
 - Impact of being treated as a primary offering:
 - Investors are deemed to be underwriters, and would need to conduct greater due diligence.
 - The company could not use an S-3 registration statement unless it had a public float of at least \$75 million.
 - Inability to rely on Rule 144 for resales as “statutory underwriters.”
 - Current trend for smaller companies is smaller deals and multiple registration statements.
 - SEC may treat APO transactions with more flexibility.

Current Issues in PIPE Transactions

- Current SEC proposals under consideration could significantly affect the PIPE market:
 - Make S-3 registration statements available for use by all issuers.
 - Reduce the holding period for Rule 144 sales from one year to six months.