VIII. Finance, Mergers, and Acquisitions

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A. Introduction

In early 2013, Mississippi joined the ranks of states enacting special purpose securitization legislation. Perhaps the most interesting development in the past year in a utility merger transaction was the post-closing fallout in the merger between Duke Energy Corp. (Duke Energy) and Progress Energy Inc. (Progress Energy). The dismissal of William E. Johnson as chief executive officer within hours of the consummation of the merger resulted in a political backlash in North Carolina and a set of additional compromises on the part of Duke Energy with various stakeholders. On the regulatory front, the Securities and Exchange Commission (SEC) and the Municipal Securities Rulemaking Board (MSRB) followed up on the SEC's previously announced enhanced focus on the municipal securities markets. In addition, the SEC proposed rules to implement the Jumpstart Our Business Startups Act[1] (JOBS Act) and to implement the conflict minerals provisions under the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (Dodd-Frank Act).[2]

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1. Jumpstart Our Business Startups Act (JOBS Act), Pub. L. No. 112-106, 126 Stat. 306 (2012), *available at* http://www.gpo.gov/fdsys/pkg/PLAW-112publ106/pdf/PLAW-112publ106.pdf.

2. Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (Dodd-Frank Act), Pub. L. No. 111-203, 124 Stat. 1376, *available at* http://www.gpo.gov/fdsys/pkg/PLAW-111publ203/pdf/PLAW-111publ203.pdf.

B. Securitization Developments

1. Mississippi Securitization Legislation[3]

On February 26, 2013, Mississippi Governor Phil Bryant signed two bills into law, House Bill 894[4] and House Bill 1134,[5] codifying a settlement between the Mississippi Public Service Commission (MPSC) and Mississippi Power Company regarding Mississippi Power's multibillion-dollar Kemper County power plant project. House Bill 894 allows Mississippi Power to establish a rate schedule for up to ten years to recover costs of the Kemper County plant, while House Bill 1134 allows the company to create a special-purpose entity to issue up to $1 billion in bonds to pay for a portion of the cost of construction of the plant.

Under a 2008 law, Mississippi Power is allowed to recover the cost of the plant through rate increases prior to the facility being built. According to Mississippi Power, House Bill 1134 is a way to give the company more flexibility in its financing of the plant's costs. Mississippi Power estimates customers could save between $1 billion and $1.5 billion under this securitized financing because the company would not seek a return on equity through base rate increases on the securitized portion.

The utility anticipates filing with the MPSC for authorization to issue rate reduction bonds to finance Kemper-related costs, as authorized under House Bill 1134. That bill allows Mississippi Power, with MPSC approval, to issue up to $1 billion of rate reduction bonds to finance construction costs of the Kemper County plant above the base cost cap established by the MPSC. Customers would be obligated to repay the bond debt, but the utility would not be permitted to collect any return on equity for the securitized amount. The $2.4 billion cap on total base rate does not cover other parts of the project outside of the plant, including a related mine and pipeline.

The Sierra Club has indicated that it will likely challenge the constitutionality of House Bills 894 and 1134.

C. Regulatory Developments

1. MSRB Rule G-17

The MSRB released an interpretative notice (Notice 2012-25)[6] requiring municipal underwriters to provide written, "deal specific" disclosure to state and local government issuers designed to ensure that such issuers understand

3. *Bryant Signs Mississippi Power's Kemper Legislation*, Energy Cent., Feb. 26, 2013.

4. Full text of the legislation is available at http://openstates.org/ms/bills/2013/HB894/documents/MSD00052950/.

5. Full text of the legislation is available at http://openstates.org/ms/bills/2013/HB1134/documents/MSD00052951/.

6. *Interpretive Notice Concerning the Application of MSRB Rule G-17 to Underwriters of Municipal Securities*, Mun. Sec. Rulemaking Bd. (Aug. 2, 2012), http://www.msrb.org/Rules-and-Interpretations/MSRB-Rules/General/Rule-G-17.aspx?tab=2.

the limits of an underwriter's obligations to an issuer and the circumstances under which the underwriter has interests that may conflict with the interests of the issuer. The Notice, interpreting underwriter responsibilities under MSRB Rule G-17, became effective August 2, 2012, and governs the underwriting of all municipal securities pricing on or after that date. On July 18, 2012, in MSRB Notice 2012-38[7] (Guidance), the MSRB provided additional guidance on the implementation of the notice, which contains written guidelines, examples, and practical considerations for underwriters to take into account.

The guidance enumerates specific disclosure requirements in connection with the basic requirement of fair dealing. These disclosures must be made in writing, made near the beginning of the underwriter's engagement, and tailored to the specific transaction, including the sophistication of the issuer and the nature of the transaction. Municipal issuers must be asked to acknowledge receipt of this disclosure.

Specifically, the Notice and the Guidance, among other things, provide that

- The underwriter is required to (1) clarify that it is not a fiduciary for the issuer, (2) outline its compensation arrangements, and (3) affirmatively describe any actual or potential material conflicts of interest;
- All representations by the underwriter to the issuer must be truthful and accurate and not misrepresent or omit material facts;
- The underwriter's duty of fair dealing includes an implied representation that the price the underwriter pays to the issuer for its bonds is fair and reasonable;
- Underwriters that recommend complex municipal securities transactions (among others, variable rate demand obligations and swaps) are required to disclose all material financial risks, characteristics, incentives, and conflicts of interest related to such complex municipal products. This requirement reflects regulatory concerns that investment banks in recent years have sometimes promoted complex financing structures not fully understood by their municipal clients;
- An underwriter must have a reasonable basis for representations it makes to municipal issuers in connection with the preparation by the municipal issuer of its disclosure documents; and
- The underwriter is obligated to honor agreements for retail order periods and take measures to ensure that retail orders are bona fide.

The Securities Industries and Financial Markets Association (SIFMA) has prepared materials on the required disclosures, including a model letter with options and comments.[8] In all cases, any letter or other disclosure communication

7. *MSRB Notice 2012-38: Guidance on Implementation of Interpretive Notice Concerning the Application of MSRB Rule G-17 to Underwriters of Municipal Securities*, Mun. Sec. Rulemaking Bd. (July 18, 2012), http://www.msrb.org/Rules-and-Interpretations/Regulatory-Notices/2012/2012-38.aspx.

to an issuer should reflect the specific facts and circumstances of the transaction being undertaken.

2. Report on the Municipal Securities Market[9]

On July 31, 2012, after a two-year examination on the structure and integrity of the municipal securities market, the SEC released its Report on the Municipal Securities Market, as mandated by the Dodd-Frank Act. This report on the $3.7 trillion municipal securities market provides a detailed overview of multiple aspects of the municipal markets and offers various recommendations, focused primarily on concerns relating to disclosure requirements and the municipal securities market structure.

a. Disclosure Concerns and Recommendations

The report identifies multiple areas of concern regarding the existing disclosure practices of the municipal securities market, including disclosures in offering documents at the time of issuance; continuing disclosure practices and compliance; the timing and content of financial statements; the nature of disclosures regarding (1) derivatives, (2) pension obligations, (3) conflicts of interest, and (4) certain material relationships; and internal controls and procedures of municipal issuers. The Report makes legislative, regulatory, and structural recommendations to improve the functioning of the municipal securities markets.

i. Legislative Recommendations

The report recommends legislation to provide the SEC with the authority to establish disclosure requirements and principles and the means to enforce them. The report notes that the SEC intends to use a principles-based approach to any new disclosure authority, recognizing the diversity of the municipal market. This would allow the SEC to consider use of scaled or tiered disclosure requirements relating to content and frequency that could be tailored to the size of the issuer, type of security, frequency of the issuance, and amount of an issuer's outstanding securities.[10]

The report also recommends the elimination of the availability of exemptions from SEC registration to conduit borrowers that are not municipal entities under § 3(a)(2) of the Securities Act of 1933 (the Securities Act). The SEC stated that it would not seek the elimination of other exemptions available to conduit borrowers, such as nonprofit entities, that benefit from an exemption from registration under § 3(a)(4). However, it noted that a conduit borrower should not be exempt from registration merely because the conduit issuer through which it has access to the capital markets is entitled to an exemption as a municipal entity.

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8. The SIFMA model letter with options and comments is available at http://www.sifma.org.

9. U.S. Sec. & Exchange Comm'n, Report on the Municipal Securities Market (July 31, 2012) [hereinafter SEC Report], *available at* http://www.sec.gov/news/studies/2012/munireport073112.pdf.

10. *See id.* at 135.

The report emphasizes that many issuers do not provide timely financial information or make annual financial information available until well after the end of their fiscal year or period. In addition, the report notes the absence of a uniform requirement for municipal entities to adhere to the standards of the Governmental Accounting Standards Board when preparing financial information. In light of these concerns, the report recommends that the SEC be given explicit authority to establish the form and content of financial statements for municipal issuers issuing municipal securities, including the authority to recognize standards of a private-sector body, over which the SEC has authority, as generally accepted for the purposes of federal securities laws. The SEC also seeks the authority to require municipal securities issuers to have their financial statements audited by either an independent or state auditor.

The report cites compliance with continuing disclosure filings as an area of concern, noting that compliance with these contractual obligations tends to weaken over time as a result of staffing changes or for other reasons. To address these concerns, the SEC seeks legislative authority "to require trustees or other entities to enforce the terms of continuing disclosure agreements."[11] In addition, the SEC suggests a safe harbor provision against private rights of action for forward-looking information that would be available only to municipal issuers that are subject to and current in their ongoing continuing disclosure requirements.

The report suggests legislation to amend the Internal Revenue Code to permit the IRS to disclose tax return information to the SEC and its staff in connection with a civil enforcement action under the federal securities laws. This would allow enforcement in the area of suspected securities fraud to be more consistent, comprehensive, and timely.

ii. Regulatory Recommendations

In addition to the legislative recommendations, the report also makes regulatory recommendations to address the SEC's disclosure concerns. These include the SEC hosting an annual conference on municipal securities markets and the release of updated interpretative guidance. The report also notes that, if the necessary legislative authority is not obtained, the SEC would consider amending Rule 15c2-12[12] under the Securities Exchange Act of 1934 (the Exchange Act) to address various disclosure concerns, such as (1) amending the definition of "final official statement" to include certain required disclosures about the offering; (2) mandating specific disclosures in official statements and ongoing disclosures; and (3) addressing noncompliance by requiring issuers to "have disclosure policies and procedures in place regarding their disclosure obligations,

11. *Id.* at 138.

12. 17 C.F.R. § 240.15c2-12, *available at* http://cfr.regstoday.com/17cfr240.aspx#17_CFR_240p15C2d12.

including those arising under continuing disclosure undertakings."[13] Finally, the report notes that the SEC will continue to work with the MSRB in identifying potential new rules or rule changes.

iii. Market-Based Recommendations

The report suggests several areas where it would be useful for the industry to expand and develop best practices guidelines. These include (1) disclosure policies and procedures for primary and ongoing disclosure, (2) availability of interim financial information, and (3) improved timeliness of financial information both in primary offerings and on an annual basis.

b. Market Structure Concerns and Recommendations

In addition to the concerns related to disclosure requirements, the report also identifies concerns related to the market structure of the municipal securities market. The primary market structure concern cited in the report is the lack of transparency.

To address pre-trade price transparency, and provide access to firm bid and ask quotations, the report notes that the SEC "could consider amendments to Regulation ATS[14] to require an alternative trading system (ATS) with material transaction or dollar volume in municipal securities to publicly disseminate its best bid and offer prices and, on a delayed and non-attributable basis, responses to 'bids wanted' auctions."[15] The report also suggests that the MSRB should draft new rules that require "a broker's broker with material transaction or dollar volume in municipal securities to publicly disseminate the best bid and offer prices on any electronic network it operates and, on a delayed and non-attributable basis, responses to 'bids wanted' auctions."[16]

To address post-trade price transparency, such as the fact that institutional investors tend to have access to a variety of sources of pricing information for municipal securities while retail investors do not, the report recommends the MSRB consider requiring municipal bond dealers to report yield spread information to the MSRB's real-time transactions reporting system, in addition to existing interest rate, price, and yield data. The report further recommends that the MSRB promptly pursue enhancements to its Electronic Municipal Market Access system, such as improved search functionality. Education initiatives for retail investors by the SEC and MSRB are also recommended to address this issue.

The report also recommends that the MSRB consider pursuing other initiatives to promote price transparency.

13. SEC Report, *supra* note 9, at 140.
14. 17 C.F.R. § 242.300 et seq., *available at* http://cfr.regstoday.com/17cfr242.aspx#17_CFR_242pRegulation_ATS.
15. SEC Report, *supra* note 9, at 143.
16. *See id.* at 144.

3. Conflict Minerals

On August 22, 2012, the SEC voted to adopt new rules implementing the conflict minerals requirements of § 1502 of the Dodd-Frank Act.[17] The Dodd-Frank Act added § 13(p) to the Exchange Act, which requires SEC-reporting companies to perform due diligence and make disclosures if they are involved in manufacturing products containing conflict minerals.

Under § 1502(e)(4) of the Dodd-Frank Act, "conflict minerals" are defined as

> columbite-tantalite, also known as coltan (the metal ore from which tantalum is extracted); cassiterite (the metal ore from which tin is extracted); gold; wolframite (the metal ore from which tungsten is extracted); or their derivatives; or any other mineral or its derivatives determined by the Secretary of State to be financing conflict in the Democratic Republic of the Congo [the DRC] or an adjoining country.[18]

Section 1502(e)(1) of the Dodd-Frank Act defines "adjoining country" as "a country that shares an internationally recognized border with the DRC, which presently includes Angola, Burundi, Central African Republic, the Republic of the Congo, Rwanda, South Sudan, Tanzania, Uganda, and Zambia."[19] The DRC, together with the adjoining countries, are the "Covered Countries." The SEC has estimated that approximately 6,000 issuers will be subject to the new disclosure requirements under these rules.

a. Determining Whether the Rules Apply

Rule 13p-1 under the Exchange Act requires all SEC registrants, including foreign private issuers, "having conflict minerals that are necessary to the functionality or production of a product manufactured or contracted by that registrant to be manufactured" to file new Form SD, which, depending on the facts and circumstances, can entail short-form reporting or a long-form audited disclosure. Form SD is required for calendar years without regard to an issuer's fiscal year; the first report is required by May 31, 2014. Although neither Rule 13p-1 nor Form SD defines "necessary to the functionality or production of a product," the SEC Adopting Release lists considerations to help a company determine if conflict minerals are necessary for the functionality of a product, including

- Whether a conflict mineral is contained in and intentionally added to the product or any component of the product and is not a naturally occurring by-product;
- Whether a conflict mineral is necessary to the product's generally expected function, use or purpose; and

17. SEC. & EXCHANGE COMM'N, RELEASE NO. 34-67716, CONFLICT MINERALS FINAL RULE (NOV. 13, 2012) [ADOPTING RELEASE], http://www.sec.gov/rules/final/2012/34-67716.pdf.
18. *Id.* at 6 n.6.
19. *Id.* n.7.

- If a conflict mineral is incorporated for purposes of ornamentation, decoration or embellishment, whether the primary purpose of the product is ornamentation or decoration.[20]

The Adopting Release also lists considerations for determining whether conflict minerals are necessary to the production of a product, including whether (1) a conflict mineral is contained in the product and intentionally added in the product's production process, including the production process of any component of the product; and (2) the conflict mineral is necessary to produce the product.[21] There is no de minimis exception under Rule 13p-1.

In addition to determining whether conflict minerals are necessary for the functionality or production of a product, the application of these new rules to an issuer also hinges on whether the company "manufactures or contracts to manufacture" a product. Again, neither Rule 13p-1 nor Form SD defines "manufacture or contract to manufacture." However, the SEC notes that this includes any situation where the company has some actual influence over the product's manufacture, but does not apply to situations where a company only services, maintains, or repairs a product. The determination of whether a company "contracts to manufacture" depends on a fact-specific determination based on the "degree of influence exercised by the issuer on the manufacturing of the product based on the individual facts and circumstances surrounding an issuer's business and industry."[22] An issuer would not be deemed to be "contracting to manufacture" a product if its actions do not go beyond

- specifying or negotiating contractual terms with a manufacturer that do not directly relate to the manufacturing of the product, such as training or technical support, price, insurance, indemnity, intellectual property rights, dispute resolution, or other like terms or conditions concerning the product, unless the issuer specifies or negotiates taking these actions so as to exercise a degree of influence over the manufacturing of the product that is practically equivalent to contracting on terms that directly relate to the manufacturing of the product;
- affixing its brand, marks, logo, or label to a generic product manufactured by a third party; or
- servicing, maintaining, or repairing a product manufactured by a third party.[23]

Stockpiles of materials or components refined or smelted prior to January 1, 2013, are considered "outside of the supply chain" and therefore not subject to Rule 13p-1. Additionally, a company engaged in mining will not be deemed to be engaged in manufacturing or contracting to manufacture minerals unless the company engages in manufacturing as well.

20. *Id.* at 22.
21. *Id.*
22. *Id.* at 62.
23. *Id.* at 65.

If a company determines that conflict minerals are not necessary to the functionality or production of a product it manufactures or has contracted to manufacture, disclosure is not required and no further action needed. However, if a company determines that conflict minerals are necessary, the rules mandate that further action is required.

b. Application of the Rules

If an issuer determines that conflict minerals are necessary, the rules require the company to conduct a good faith reasonable "country of origin inquiry" to determine whether the minerals originated in one of the Covered Countries. The concept of a reasonable "country of origin inquiry" is not defined in either Rule 13p-1 or Form SD. Although the Adopting Release notes that a reasonable inquiry "can differ among issuers based on the issuer's size, products, relationships with suppliers, or other factors," the inquiry must be "designed to determine whether the issuer's conflict minerals did originate" in one of the Covered Countries, or instead came from recycled or scrap materials; the inquiry must be performed in good faith.[24] The SEC has noted that this standard is satisfied if the company "seeks and obtains reasonably reliable representations indicating the facility at which its conflict minerals were processed and demonstrating that those conflict minerals did not originate in the Covered Countries or came from recycled or scrap sources."[25] These representations can "come either directly from that facility or indirectly through the issuer's immediate suppliers, but the issuer must have a reason to believe these representations are true given the facts and circumstances surrounding those representations."[26]

If an issuer, based on the reasonable "country of origin inquiry," concludes that its conflict minerals either did not originate in a Covered Country or came from recycled or scrap sources, and if the issuer has no reason to believe that the minerals may have originated in a Covered Country, the issuer must disclose its conclusion and the inquiry process it used to arrive at this conclusion on Form SD, filed with the SEC, and make this disclosure available on its website. The conflict minerals disclosure does not require an independent private-sector audit, and the determination does not need to be certain, but the process must be reasonably designed and performed in good faith.

However, if an issuer, based on the reasonable "country of origin inquiry," concludes that its conflict minerals originated in a Covered Country, or has reason to believe that conflict minerals in its supply chain originates in a Covered Country, the issuer must disclose its conclusion on Form SD, submit a "conflict minerals report" to the SEC, furnish it as an exhibit to Form SD, and post the report on its website.

The report must describe measures taken by the issuer to "exercise due diligence" on the source and chain of custody of its conflict minerals, including

24. *Id.* at 147–48.
25. *Id.* at 148.
26. *Id.*

an independent private-sector audit. The diligence review must conform to a nationally or internationally recognized framework, such as those approved by the Organisation for Economic Cooperation and Development (OECD Due Diligence Guidelines). In the report, the issuer must identify its independent private-sector auditor, certify that it obtained an independent private-sector audit of the report, and provide the audit report as part of the conflict minerals report. The purpose of the audit is to determine whether the design and description of the company's due diligence measures are in conformity with the framework actually used by the company.

If a company determines through due diligence that its minerals are "DRC Conflict Free," i.e., meaning that the minerals that originated out of the Covered Countries did not finance or benefit armed groups in the these countries, the above requirements are the only requirements for the conflict minerals report. However, if the minerals are not found to be DRC Conflict Free, in addition to the audit and certification requirements, the report must also describe

- The products manufactured or contracted to be manufactured with conflict minerals that have not been found to be DRC Conflict Free;
- The facilities used to process the conflict minerals in those products;
- The conflict minerals' country of origin; and
- The efforts used to identify the mine or location of origin with the greatest possible specificity.

The SEC has determined that conflict minerals obtained from recycled or scrap sources, rather than mined, fall outside the purpose of § 1502 of the Dodd-Frank Act; therefore, issuers using such materials have less exhaustive disclosure obligations. If, after performing a reasonable "country of origin inquiry," an issuer knows or reasonably believes that its conflict minerals are from scrap or recycled sources, the company must still file Form SD but may note its belief that its conflict minerals were obtained from recycled or scrap sources as well the basis for such belief. A company that cannot reasonably conclude after its inquiry that its gold is from recycled or scrap sources is required to undertake due diligence in accordance with OECD Due Diligence Guidelines and have its conflict minerals report audited.[27]

For 2013 and 2014 (or 2013–2016 for smaller reporting companies), issuers can omit the independent private-sector audit report from its conflict minerals report with respect to any conflict minerals that are found to be "DRC Conflict Undeterminable." Such a finding can occur when either

- A company cannot factually determine, after a reasonable "country of origin inquiry" and supply chain due diligence, whether the conflict minerals

27. Until a due diligence framework is developed for conflict minerals other than gold, a company that cannot reasonably conclude that its other conflict minerals are from recycled or scrap sources must describe the due diligence measures it took to reach this conclusion, but it is not required to obtain an independent private-sector audit.

in the supply chain that originated in a Covered Country financed or benefitted arms groups in such countries; or

- A company cannot determine, after these steps, whether it has reason to believe the conflict minerals used in its supply chain may have originated in a Covered Country.

However, beginning with 2015 (or 2017 for smaller reporting companies), an issuer with DRC Conflict Undeterminable minerals must describe the products as not having been found DRC Conflict Free and obtain an independent private-sector audit.

4. SEC JOBS Act Implementation

On April 5, 2012, the JOBS Act, a series of regulatory reforms intended to ease the capital formation process in private offerings, was enacted. Section 201(a) of the JOBS Act required the SEC to (1) revise its rules to remove the prohibition against general solicitation and general advertising in private offerings under Rule 506 of Regulation D[28] of the Securities Act, provided that all purchasers of the securities are or reasonably believed to be accredited investors, and the issuer has taken reasonable steps to verify that all purchasers of the securities are accredited investors; and (2) revise Rule 144A[29] under the Securities Act to provide that securities sold pursuant to Rule 144A may be offered to persons other than qualified institutional buyers, including through general solicitation and general advertising, as long as the seller has a reasonable belief that all purchasers in the offering are qualified institutional buyers.[30] The JOBS Act also amended § 4 of the Securities Act to provide that offerings made in compliance with Rule 506 will not be deemed public offerings as a result of general solicitation or advertising. On August 29, 2012, as required by the JOBS Act, the SEC proposed amendments to Rule 506 and Rule 144A.

a. Rule 506

Rule 506 is a nonexclusive safe harbor permitting unregistered sales of securities to an unlimited number of accredited investors and a limited number of non-accredited investors. Reliance upon Rule 506 is subject to a number of conditions, including a condition that the issuer not offer or sell the securities through any form of general solicitation. Instead of altering or eliminating the current Rule 506 regime, the proposed amendments would establish a second type of offering under new Rule 506(c) that would allow general solicitation.

28. 17 C.F.R. § 230.506, *available at* http://www.ecfr.gov/cgi-bin/text-idx?c=ecfr&rgn=div5&view=text&node=17:2.0.1.1.12&idno=17?17:2.0.1.1.12.0.42.181.

29. 17 C.F.R. § 230.144A, *available at* http://www.ecfr.gov/cgi-bin/text-idx?c=ecfr&rgn=div5&view=text&node=17:2.0.1.1.12&idno=17?17:2.0.1.1.12.0.32.29.

30. Sec. & Exchange Comm'n, Release No. 33-9354, Eliminating the Prohibition Against General Solicitation and General Advertising in Rule 506 and Rule 144A Offerings (Aug. 29, 2012), http://www.sec.gov/rules/proposed/2012/33-9354.pdf.

Under new Rule 506(c), an issuer would be permitted to utilize general solicitation and advertising in connection with a Rule 506 offering, provided that

- The issuer takes reasonable steps to verify that all purchasers of the securities sold in the offering are accredited investors;
- At the time of the sale of the securities, all of the purchasers are, or the issuer reasonably believes them to be, accredited investors; and
- All terms and conditions of existing Rules 501 (definitions), 502(a) (integration restriction), 502(d) (resale limitations), and 503 (notice of sales) of Regulation D are satisfied.[31]

The proposed amendments do not define what would constitute "reasonable steps to verify" a purchaser's accredited investor status and do not require specific verification methods. Instead, the SEC notes that an analysis of whether the steps taken are reasonable would be an objective determination based on the facts and circumstances of each transaction. The SEC did identify several examples of factors to be considered by issuers in this analysis, including

- The nature of the purchaser and the type of accredited investor that the purchaser claims to be;
- The amount and type of information that the issuer has about the purchaser; and
- The nature of the offering, such as the manner in which the purchaser was solicited to participate in the offering, and the terms of the offering, such as the minimum investment amount.

The SEC noted that these factors are interconnected; stronger support under one factor indicating that a purchaser is an accredited investor results in fewer steps needed by the issuer to conclude that it has taken reasonable steps to verify the purchaser's accredited investor status, and vice versa. Examples of verification techniques include (1) publicly available information with a local, state, or federal regulatory body; (2) third-party information, such as W-2s, that provide reasonably reliable evidence that a person is an accredited investor; and (3) verification by a third party, such as an accountant, attorney, or broker-dealer, on whom the issuer has a reasonable basis to rely.

The SEC noted that reliance on check-the-box style investor questionnaires to assist in determining accredited investor status, absent other information would not be reasonable in the context of a freely accessible website solicitation, widely disseminated e-mail, or social media solicitation. In contrast, the SEC noted that if a minimum investment requirement is high enough that only accredited investors could reasonably be expected to meet it, it may be reasonable for the issuer to

31. However, Rule 501(b) (which requires specified information disclosures to nonaccredited investors) and 501(c) (which prohibits general solicitation and advertising in connection with a Regulation D offering) would not apply.

take no steps to verify accredited investor status beyond confirming that the purchaser's cash investment is not being financed by the issuer or a third party.

The SEC did not propose to amend the definition of accredited investor; thus, the reasonable belief standard in Rule 501(a) remains intact. Therefore, in the event that an issuer sold securities under new Rule 506(c) to a person who was not in fact an accredited investor, the issuer would not lose the ability to rely on this proposed exemption for that offering, as long as it reasonably believed that all purchasers were accredited investors under the existing standards and had taken reasonable steps to verify their status as required under the proposed rules. Although no specific recordkeeping requirements were proposed in the release, the SEC noted that any issuer claiming the exemption has the burden of showing that it is entitled to the exemption. The SEC noted the importance of retaining adequate records.

b. Form D

The SEC also proposed to amend Form D to require issuers to specify whether the offering was made without general solicitation or in reliance on the new alternative approach permitting general solicitation. The revised form would add a separate box for issuers to check if they are claiming the new Rule 506 exemption, allowing the SEC to monitor the use of the safe harbor and related practices and potentially engage in additional rulemaking.

c. Rule 144A

Rule 144A is a nonexclusive safe harbor permitting resales of restricted securities to qualified institutional buyers (QIBs) without registration under the Securities Act. Although Rule 144A does not restrict general solicitation, the condition that an offer must be made only to QIBs has a practical effect of limiting offers to non-QIBs and is tantamount to a prohibition on general solicitation. The SEC's proposed amendments to Rule 144A remove the references to the words "offered" and "offeree," with the amended rule simply requiring that the securities be sold only to QIBs or to a person that the seller and any person acting on behalf of the seller reasonably believe is a QIB. The practical impact of this change is that Rule 144A offerings would be able to allow general solicitation.

d. Implications Under Other Securities Laws: Investment Company Act and Regulation S

i. Investment Company Act

The SEC confirmed in the proposing release that privately offered funds may make a general solicitation under new Rule 506(c) without losing either of the § 3(c)(1) or 3(c)(7) exclusions under the Investment Company Act of 1940, as amended.[32] These exclusions are currently not available to issuers

32. Investment Company Act of 1940, Pub. L. No. 76-768, as amended through Pipeline Safety, Regulatory Certainty, and Job Creation Act of 2011, Pub. L. No. 112-90, 125 Stat. 1904 (2012), *available at* http://www.sec.gov/about/laws/ica40.pdf.

that are making or proposing a public offering and are the exclusions most commonly relied upon by private funds. As a result, if the proposed rule is adopted in its current form, private funds would be permitted to conduct an offering using general solicitation in compliance with Rule 506(c) without losing the benefit of the § 3(c)(1) or 3(c)(7) exclusions from investment company status.

ii. Regulation S

The SEC did not propose any changes to Regulation S[33] under the Securities Act or its prohibition on "directed selling efforts" in the United States, which is often seen as similar to general solicitation. However, the SEC confirmed that, under the proposed amendments, an offshore offering that is conducted in compliance with Regulation S would not be integrated with a concurrent domestic unregistered offering that is conducted in compliance with Rule 506 or Rule 144A.

D. Announced Transactions

1. Fortis Inc. and CH Energy Group, Inc.

On February 21, 2012, Fortis Inc. (Fortis) announced that it had reached an agreement to acquire CH Energy Group, Inc. (CH Energy) for $65 per share in cash and an aggregate purchase price of $1.5 billion, including the assumption of approximately $500 million of debt, representing an approximately 10.5 percent premium above the then most recent closing price of CH Energy shares. Fortis is the largest investor-owned distribution utility in Canada, with total assets of approximately $14 billion, serving more than 2,000,000 gas and electricity customers.[34]

CH Energy's main business is its subsidiary, Central Hudson Gas & Electric Corporation (Central Hudson), a regulated transmission and distribution utility serving approximately 300,000 electric and 75,000 natural gas customers in eight counties of New York State's Mid-Hudson River Valley. CH Energy also owns and operates Central Hudson Enterprises Corporation, a nonregulated fuel delivery business serving approximately 56,000 customers in the Mid-Atlantic region. Following closing of the acquisition, the total assets of Fortis are expected to be approximately $17 billion.[35]

On June 19, 2012, shareholders of CH Energy approved the transaction.[36] On July 5, 2012, the Federal Energy Regulatory Commission (FERC) approved the transaction, finding that the transaction was consistent with the public interest.[37]

33. 17 C.F.R. §§ 230.901–904, *available at* http://cfr.regstoday.com/17cfr230.aspx#17_CFR_230pRegulation_S.

34. Press Release, Fortis Inc., Fortis Inc. to Acquire CH Energy Group, Inc. for US$1.5 Billion (Feb. 21, 2012), http://www.fortisinc.com/Attachments/MediaReleases/535.pdf.

35. *Id.*

36. Press Release, Fortis Inc., Fortis Inc. Acquisition of CH Energy Group, Inc. Approved by Shareholders (June 19, 2012), http://www.fortisinc.com/Attachments/MediaReleases/545.pdf.

37. Press Release, Fortis Inc., Fortis Inc. and CH Energy Group, Inc. Transaction Approved by Federal Energy Regulatory Commission (July 5, 2012), http://www.fortisinc.com/Attachments/MediaReleases/551.pdf.

Also in July, 2012, the Committee on Foreign Investment in the United States approved the transaction. On October 4, 2012, Fortis and CH Energy announced the expiration of the waiting period under the Hart-Scott-Rodino Antitrust Improvements Act of 1976 (HSR) in connection with the transaction.[38]

On January 28, 2013, Fortis announced that it had filed a settlement agreement with the New York State Public Service Commission (NYPSC) and certain intervenors regarding the acquisition of Central Hudson. The settlement agreement included provisions mandating (1) nearly $50 million to fund customer and community benefits; (2) a one-year electric and natural gas customer delivery rate freeze; and (3) certain other customer protections, including the continuation of Central Hudson as a stand-alone utility company. The settlement agreement will moderate future customer rate increases by requiring Fortis to provide Central Hudson with $35 million to cover expenses normally recovered in customer rates, including restoration expenses related to the October 2012 Superstorm Sandy and tropical storm Irene. In addition, Central Hudson customers will save a guaranteed $9.25 million over five years due to "synergy savings." Finally, the settlement agreement requires the establishment of a $5 million Customer Benefit Fund for economic development and low-income assistance programs for communities and residents of the Mid-Hudson Valley.[39]

Central Hudson will maintain its name and Poughkeepsie headquarters. In addition, it will maintain all of its employees for at least two years. Within one year, the board of directors of Central Hudson will transition to a majority of independent directors, increase membership from the Hudson Valley and New York State, and include representatives of Fortis.[40]

Other signatories to the settlement agreement include the staff of the New York State Department of Public Service, multiple intervenors, and the Utility Intervention Unit of the New York State Department of State. The settlement agreement indicates that the acquisition is in the public interest, and the aforementioned parties recommend approval of the settlement agreement by the NYPSC.[41] Closing of the acquisition was expected to take place during the second quarter of 2013, subject to NYPSC approval.[42]

2. Duke Energy Corp. and Progress Energy Inc.

On November 29, 2012, Duke Energy filed a settlement agreement with the North Carolina Utilities Commission (NCUC). The settlement agreement re-

38. Press Release, Fortis Inc., Fortis Inc. and CH Energy Group, Inc. Announce Expiration of Hart-Scott-Rodino Waiting Period (Oct. 4, 2012), http://www.fortisinc.com/Attachments/MediaReleases/555.pdf.

39. N.Y. Pub. Serv. Comm'n, Joint Proposal for Comm'n Approval of the Acquisition of CH Energy Grp., Inc. by Fortis Inc. & Related Transaction, Case 12-M-0192 (Jan. 25, 2013).

40. *Id.*

41. *Id.*

42. Press Release, Fortis Inc., Fortis and Central Hudson File Settlement Agreement: Includes Substantive Customer Benefits and Protections (Jan. 28, 2013), http://www.fortisinc.com/Attachments/MediaReleases/562.pdf.

solved all issues related to the matters under investigation by the NCUC regarding the change in president and chief executive officer following the completion of the merger between Duke Energy and Progress Energy on July 2, 2012. Under the terms of the agreement, Duke Energy agreed to the following key provisions:

- Duke Energy provided additional merger commitments, including (1) maintaining at least 1,000 employees in Raleigh, North Carolina; (2) guaranteeing an additional $25 million in fuel and fuel-related cost savings to North Carolina customers; and (3) making $5 million in additional contributions to support workforce development and low-income assistance in North Carolina;
- Duke Energy made certain personnel changes, including moving Lloyd Yates, currently Executive Vice President, Customer Operations, into the position of Executive Vice President, Regulated Utilities, and appointing a new general counsel;
- Duke Energy created a special committee on the Board to oversee the recommendation of a successor to current Chairman, President, and CEO Jim Rogers upon his retirement, and the search for two new Board members;
- Duke Energy agreed to defer filing a general rate case by Duke Energy Carolinas, LLC in North Carolina until February 2013, with the understanding that it will be allowed to defer the depreciation and operation costs of new generation incurred from the commercial operation of such new generation until the effective date of new base rates; and
- Duke Energy will retain the former general counsel of Progress Energy to advise the company for two years on regulatory and legislative matters in North Carolina.

Duke Energy's current general counsel and Executive Vice President, Regulated Utilities, assumed new leadership roles. Duke Energy will also provide proportional fuel, fuel-related, workforce, and low-income assistance financial benefits to its South Carolina customers, expected to total between $8 and $9 million, consistent with the recent merger-related commitments to customers in the state.[43]

On December 3, 2012, Duke Energy announced that it had also reached a settlement with the North Carolina attorney general that includes, among other things, the following:

- The attorney general will not object to the settlement reached with the NCUC;
- The attorney general preserves all rights in future Duke Energy rate cases in North Carolina;
- The Regulatory Policy and Operations Committee of the Duke Energy Board of Directors will meet with the attorney general periodically;

43. Press Release, Duke Energy, Duke Energy Reaches Settlement Agreement with NCUC Staff and NC Public Staff (Nov. 29, 2012), http://www.duke-energy.com/news/releases/2012112902.asp.

- Duke Energy will retain an independent entity to survey North Carolina customers about their satisfaction with their electric service and how it could be improved, and report the results to the attorney general within one year;
- Duke Energy will retain an independent entity to survey its employees regarding merger integration and post-merger operations and report the results to the attorney general within two years;
- Duke Energy will designate a liaison in the company to communicate with the attorney general on customer-related information; and
- Duke Energy will pay $250,000 to the attorney general's office to defray fees and expenses related to the post-merger investigation.[44]

The North Carolina Waste Awareness and Reduction Network has challenged the NCUC approval of the merger in the North Carolina Court of Appeals and has asked the state attorney general to reopen his investigation.

3. Entergy Corporation and ITC Holdings

In connection with the proposed merger between Entergy Corporation (Entergy) and ITC Holdings Corp. (ITC) announced on December 5, 2011, Entergy and ITC have proceeded to seek the various regulatory approvals required to consummate the transaction. The multistate and federal regulatory approval process began in September 2012 with filings with the Louisiana Public Service Commission (LPSC) and the New Orleans City Council.[45]

Entergy Arkansas, Inc. (EAI), ITC, and ITC Midsouth LLC filed a request on September 28, 2012, with the Arkansas Public Service Commission (Arkansas PSC) to spin off the Arkansas electric transmission business and merge it into the subsidiary of ITC. On October 5, 2012, Entergy Mississippi, Inc., ITC, and ITC Midsouth filed a request with the MPSC to spin off its Mississippi electric transmission business and merge into the subsidiary of ITC.[46] EAI, ITC, and ITC Midsouth filed for approval of the transaction in Missouri on February 15, 2013. Entergy Texas, Inc., ITC, and ITC Midsouth then filed with the Public Utility Commission of Texas on February 19, 2013.

On September 24, 2012, ITC and Entergy filed a joint application with FERC seeking approval of the spinoff and merger under §§ 203, 205, and 305 of the Federal Power Act (FPA). On October 31, 2012, Entergy and ITC filed applications under FPA § 204 seeking FERC approval of certain debt financings re-

44. Press Release, Duke Energy, Duke Energy Reaches Settlement Agreement with North Carolina Attorney General (Dec. 3, 2012), http://www.duke-energy.com/news/releases/2012120301.asp.

45. Press Release, ITC Holdings Corp., Entergy and ITC Continue Transaction Approval Process with Arkansas Public Service Commission Filing (Sept. 28, 2012), http://www.itc-holdings.com/itc-entergy/news/item/342-entergy-and-itc-continue-transaction-approval-process-with-arkansas-public-service-commission-filing.html.

46. Press Release, ITC Holdings Corp., Entergy and ITC Continue Transaction Approval Process with Mississippi Public Service Commission Filing (Oct. 5, 2012), http://www.itc-holdings.com/itc-entergy/news/item/345-entergy-and-itc-continue-transaction-approval-process-with-mississippi-public-service-commission-filing.html.

quired to effectuate the transaction. The public utility commissions of Arkansas, Louisiana, and Texas; the Tennessee Valley Authority; and various other stakeholders have filed interventions in Entergy and ITC's § 305 proceeding with FERC.

On December 14, 2012, Entergy and ITC each filed a premerger notification under HSR. The waiting period under HSR expired on January 14, 2013.

In connection with the filings listed above, in testimony filed on April 10, 2013, the LPSC staff urged the commission to reject the current plan without changes, such as new stipulations guaranteeing the LPSC the ability to oversee and limit future cost increases to Louisiana ratepayers, arguing that the companies have underestimated rate hikes that the deal will impose on Entergy's Louisiana customers.[47] In testimony filed with the Arkansas PSC in April 2013, the staff of the Arkansas PSC and the Arkansas attorney general registered their opposition to the proposed transaction.[48]

ITC's Registration Statement on Form S-4 was filed with the SEC on September 25, 2012. It registers shares of ITC common stock to be issued to Entergy shareholders but has not yet been declared effective. On April 16, 2013, ITC announced that its shareholders approved the transaction at a special meeting of the shareholders.[49] The companies are targeting a transaction close in 2013, pending receipt of all required regulatory approvals and satisfaction of other closing conditions.[50]

47. Jeff Beattie, *Louisiana PSC Staff Sour on Entergy Grid Sale to ITC*, IHS ENERGY DAILY, Apr. 22, 2013.

48. IHS ENERGY DAILY, Apr. 23, 2013.

49. ENERGY FIN. DAILY, Apr. 17, 2013.

50. ITC Press Release, *supra* note 46.