

SEC Delays Enforcement of Rule 15c2-11 Compliance

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In 2021, the Securities and Exchange Commission (SEC) took the industry off-guard by announcing its new position that Rule 15c2-11 of the Securities Exchange Act of 1934 (Rule) and its amendments apply to fixed-income securities, which had previously not been subject to enforcement actions under the Rule. The amendments to the Rule in September 2020, from which this interpretation arose, requires brokers and dealers in deriving their quotes to be published in a quotation medium to review documents that are “current” and “publicly available.” On November 30, 2022, the SEC issued a No-Action Letter delaying full compliance with these requirements of the amendments to the Rule from January 3, 2023 to January 4, 2025.

Phased-In Compliance

Despite the No-Action Letter, the SEC staff’s interpretation of the amendments to the Rule can have a significant impact on issuers of fixed-income securities, in particular those offering fixed-income securities pursuant to Rule 144A. As noted above, the most recent No-Action Letter on Rule 15c2-11 enforcement delayed full compliance with the requirements of the amendments to the Rule. Instead, the SEC staff is phasing in compliance with the Rule in three phases. Notably, Phase 1 currently provides an exemption from enforcement under the Rule for securities being offered pursuant to Rule 144A. However, in Phase 2, securities being offered pursuant to Rule 144A will no longer be exempt from enforcement under the Rule. Provided that no other exemptions from compliance with the Rule apply, starting in Phase 2, issuers offering such fixed-income securities pursuant to Rule 144A would need to ensure that documents on which brokers and dealers rely are “publicly available” and remain “current” per the timelines set out by the amendments to Rule 15c2-11. In Phase 3, Rule 144A Securities would become fully subject to the Rule.

More specifically, the amendments to the Rule requires brokers and dealers to review: (i) identifying information about the issuer and the relevant security; (ii) information about the issuer’s business; and (iii) the issuer’s most recent balance sheet (as of a date less than 16 months prior) and profit

and loss and retained earnings statements for the 12 months preceding the date of the most recent balance sheet. While such information is substantially similar to the requirements of Rule 144A(d)(4), the Rule requires issuers of Rule 144A securities to make such information publicly available if they wish to permit brokers and dealers to publish quotations on their securities. Further, documents are “publicly available” if they are available on EDGAR; on the website of a state or federal agency, a qualified interdealer quotation system, a registered national securities association, a registered broker or dealer or an issuer; or through an electronic information delivery system that is generally available to the public in the primary trading market of a foreign private issuer. The extension of the Rule to require brokers and dealers to review publicly available information could create a considerable shift from normal procedures for issuers with fixed-income securities being offered pursuant to Rule 144A.

Disclosure Considerations

Issuers who are not otherwise required to disclose publicly financial statements and other information to the SEC will need to determine whether or not they are willing to make this information publicly available. Those issuers who choose to begin making this information publicly available could experience increased costs in offering and maintaining their securities, as such issuers will need to prepare specific documents and annual financial statements to be filed with the SEC (and comply with the SEC’s procedures) as opposed to making the information available only to select parties through the access-restricted measures mentioned below.

Issuers who choose not to disclose publicly this information could experience adverse impacts to their liquidity and the value of their securities, since brokers and dealers would be restricted from publishing quotations on their securities as no current, publicly available information would be available to them. Brokers and dealers also should be aware of the expiration of certain specified time periods (the “phases”) set forth in the No-Action Letter, as they will need to verify from issuers, or institute new procedures, to determine whether the documents being relied upon to publish quotations are both “current” and “publicly available.”

Retail Investors Versus Qualified Institutional Buyers

Recognizing the impacts of this new interpretation of the Rule on Rule 144A offerings, the SEC granted temporary relief from securities offered pursuant to Rule 144A; however, the industry strongly believes that this temporary relief from enforcement pursuant to the Rule should be extended permanently. The primary purpose of registering an offering of securities with the SEC is to provide a layer of protection to the unsophisticated, individual investor. The question of whether a security is being offered to the public has always turned on the position of the purchaser. Purchasers of securities being offered pursuant to Rule 144A may only be Qualified Institutional Buyers. Such market participants must own and invest at least \$100,000,000 of securities in unaffiliated issuers. No individual can be considered a Qualified Institutional Buyer, regardless of how much wealth or knowledge has been accumulated in the industry. Thus, individual investors may not purchase a security being offered pursuant to Rule 144A. Requiring an issuer offering fixed-income securities pursuant to Rule 144A to make certain documents and information publicly available does not serve to protect the unsophisticated, individual investor, since such investor is precluded from purchasing a Rule 144A security in the first place.

Additionally, in proposing Rule 144A in 1988, the level of information required to be produced in such an offering was discussed extensively. The discussions largely centered on whether any information at all needed to be provided, or basic information provided only upon request. Although most of the

commenters to Rule 144A felt that no information need be provided due to the institutional knowledge of the purchaser participating in the transaction, Rule 144A required the issuer provide certain limited information to the purchaser upon request. The Qualified Institutional Buyer knows what it wants to consider in purchasing a security and knows what to request from an issuer in making these considerations. Requiring this information be publicly available does not provide the added benefit of disclosure to these investors as they will request what they want to consider in purchasing these securities. Given that Rule 144A was adopted years after the adoption of Rule 15c2-11, the drafters of Rule 144A were able to assess whether or not the level of information required to be provided should rise to the level required pursuant to Rule 15c2-11. Ultimately, the drafters of Rule 144A decided the level of information in Rule 15c2-11 is far beyond what is required. To not only require this level of information be provided now and be publicly available, while also saying the Rule always applied to fixed-income securities, is at odds with intent and purpose Rule 144A.

The primary purpose of Rule 144A is to promote an efficient and liquid private resale market. The application of Rule 15c2-11 to the private placement market can upend the purpose of Rule 144A by increasing costs to issuers looking to offer securities pursuant to Rule 144A and decreasing liquidity for holders of these securities as they may not receive accurate quotes, if any, on their fixed-income securities. Although the No-Action Letter extended relief from Rule 15c2-11 until January 4, 2025, the industry supports permanent relief for those issuers offering securities pursuant to Rule 144A.

Additional Resources

For further reading on Rule 15c2-11 and its application to the fixed-income industry, please see the following:

The Amended Rule 15c2-11 is available [here](#).

The proposal for Rule 144A is available [here](#) on pages 3 through 25. The re-proposal for Rule 144A is available [here](#) on pages 78 through 89. The adopting release for Rule 144A is available [here](#) on pages 2 through 18.

The SEC No Action Letter from December 16, 2021 introducing the phases of compliance with the amendments to Rule 15c2-11 compliance is available [here](#).

The SEC No Action Letter from November 30, 2022 extending the duration of Phase 1 of the exemption from compliance with the amendments to Rule 15c2-11 is available [here](#).

Commentary by the Securities Industry and Financial Markets Association (SIFMA) on the history of Rule 15c2-11 and its intent is available [here](#). SIFMA commentary on the impact of the amendments to Rule 15c2-11 applying to the fixed-income industry is available [here](#).

The letter submitted by the Structured Finance Association (SFA) to the SEC regarding the potential application of Rule 15c2-11 to fixed-income securities is available [here](#).

Dylan Caffrey also contributed to this article.

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