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MANAGING YOUR BOND LIABILITIES UNDER US SECURITIES LAW: A GUIDE FOR NON-US ISSUERS

Approximately $55.3 trillion of fixed income securities are outstanding in the United States[1], including debt securities offered by non-US sovereign, investment grade and sub-investment grade corporate issuers pursuant to Rule 144A or another exemption from registration under the US Securities Act of 1933, as amended (the Securities Act).

These issuers are expected to continue tapping the debt markets in the United States for funding. While it is relatively straightforward simply to repay debt with new money, issuers often want to explore options that may achieve the goals of extending their maturity profile and/or reducing costs or interest expense in a more creative way in so-called "liability management" transactions, including, among others:

- tender offers: a "public" offer made by an issuer to repurchase all or a portion of its outstanding bonds from investors for cash; and
- exchange offers: an offer made by an issuer to repurchase its outstanding bonds in exchange for new bonds with different terms.

If US investors are approached in connection with these transactions, the US securities laws come into play. This article provides a brief overview of these US securities laws and explores how transaction structures have evolved over time in response to these laws.

US Tender Offer Rules

Fundamental guidelines for tender and exchange offers made to US holders of debt securities can be found under Section 14(e) of the US Securities Exchange Act of 1934, as amended (the Exchange Act) and Regulation 14E thereunder. Section 14(e) of the Exchange Act empowers the US Securities and Exchange Commission (the SEC) to establish rules and regulations that help minimise fraudulent, deceptive, or manipulative acts and specified practices in connection with any tender offer.

Subject to certain exemptions, Rule 14e-1 of Regulation 14E stipulates, among other procedural requirements, that tender offers:

- must remain open for a minimum of 20 business days; and

[1] Source: SJFMA, "2024 Capital Markets Fact Book" (30 July 2024), https://www.sifma.org/wp-content/uploads/2023/07/2024- SJFMA-Capital-Markets-Factbook.pdf.

- must remain open for a minimum of 10 days following either
    - a change in the percentage of the class of securities sought; or
    - a change in the consideration offered for the securities.

The anti-fraud provisions of the Exchange Act are also applicable to debt tender offers. Therefore, under Section 10(b) of the Exchange Act and Rule 10b-5 thereunder, it is unlawful to make any untrue statement of a material fact or to omit to state a material fact in connection with the purchase or sale of securities.

While the rules appear straightforward, the devil is often in the details and there is a limited amount of SEC guidance available on these topics. While many of these questions do not have universal answers, the below discussion looks at transaction structures that have been developed in the past in light of the US rules and aims to provide guidance for when similar questions emerge on subsequent tender offers.

Mitigating the 20-Business Day Requirement

For many, the requirement to keep a tender offer open for at least 20 business days (and for 10 business days after any change in price) is the biggest drawback to the US tender offer rules (and leads to US holders being excluded from offers, to the extent possible). The dynamics of the markets often mean that it is not optimal to be required to hold offers open for this long.

Early Bird/Early Settlement

The 20 business day requirement led to innovations starting in the 1980s around structuring transactions to effectively shorten the period for which the offeror has uncertainty as to acceptance levels and the closing date.

These concerns have led to widespread use of the following mechanisms:

- "Early bird" payments. These provide a "premium" tender price for holders that tender by the "early bird" date, after which tenders will only receive the "standard" tender price. Due to Rule 14e-1(b), which requires that 10 business days' notice be given of any changes in price, these are typically structured at the outset as "10+10" offers, in the sense that the early bird payment lasts for the initial 10 days, and then steps down on the eleventh day to the lower tender price. This "10+10" structure is often tested (and we are frequently asked whether the early bird price can be extended without extending the tender itself (so, effectively, the early bird would be available for 12 days, for example, and the lower price available for eight days)). Some practitioners have taken the view that this would comply with Rule 14e-1(b), as holders already have 10 days' notice of the change in price (and do not take the view that Rule 14e-1(b) requires that holders ALWAYS need 10 business days between the final expiry date of the offer and the end of the early bird period so long as the notice requirement is met).
- Early settlement. Frequently, in tender offers where there is an "early bird" period, there will also be provision for early settlement of those tenders (so any "early bird" tenders are actually paid, for example, at day 12 and any other tenders would be paid at day 21). While this can have the practical effect in a partial tender that no tenders are

accepted after the early bird date (as all of the tenders up to the cap have been accepted), this mechanism has been accepted in the market.

Accelerated Tenders

Beginning in 1986, the SEC provided targeted relief from the 20 business day offer period for certain all-cash, non-convertible, investment-grade debt tender offers, recognising that debt tender offers generally raise fewer policy concerns than equity tender offers and entail different timing considerations. In January 2015, the SEC expanded and formalised this position with a no-action letter describing the conditions under which a debt tender offer or an exchange offer may be structured to take advantage of an abbreviated five-day offer period (an abbreviated offer).[2] The conditions include that: (1) the abbreviated offer must be for "any and all" of a series of non-convertible debt securities (the any and all condition); (2) the abbreviated offer must be made by the issuer, a wholly-owned subsidiary or a parent company; and (3) in the case of an abbreviated exchange offer, the consideration must be non-convertible debt securities identical in all material respects to the securities that are the subject of the offer except for the maturity date, interest payment and record dates, redemption provisions and interest rate (which must be payable only in cash) and have a longer weighted average life to maturity (the parallel terms condition).

Under the terms of the 2015 no-action letter, an abbreviated tender offer cannot be made in a transaction combined with a consent solicitation (exit consent) or in response to, or concurrently with, a change of control or other type of extraordinary transaction involving the issuer or in combination with another concurrent offer for any other series of the issuer's securities if the effect of such concurrent offer, if consummated, would be to add obligors, guarantors or collateral (or increase the priority of liens securing such other series) or shorten the weighted average life to maturity of such other series. It also cannot be made where the issuer is in default.

While market participants generally gratefully received the 2015 no-action letter, the conditions under which an abbreviated offer may be conducted can materially limit its usefulness, particularly for exchange offers. The any and all condition for use of the accelerated tender is often the most important and leads to the most questions – issuers cannot rely on the 2015 no-action letter for partial tenders, which has led to some of the structuring that we discuss below. Likewise, practitioners have interpreted the parallel terms condition to mean that new bonds issued in exchange for existing bonds in an exchange offer must contain the same covenants, which also limits potential issuer flexibility going forward and/or the attractiveness of the transaction.

Dutch Auctions

In lieu of a fixed price tender offer, issuers may consider a so-called "Dutch Auction" tender offer, where investors are invited to bid at a price (usually within a specified range) and the issuer accepts such bids at individual prices for the level of buy-back it wishes to achieve. However, Rules 14d-10 and 13e-4(f)(8)(ii) under the Exchange Act require that the consideration paid to any holder for securities tendered in the tender offer be the highest consideration paid to any other holder in the tender offer (the best price rule).

Practice tip

For example, for SEC-registered securities, the SEC requires prompt and accurate disclosure relating to any changes in the key terms of a debt tender offer to holders of the tendered securities. Depending on the nature of the offer and the type of securities being tendered, debt tender offers by SEC registrants must be announced to the public through a combination of press releases and filings within the SEC's EDGAR system. When issuers need to utilise both press releases and SEC filings, these should be published simultaneously. This helps to ensure that all investors receive the information at the same time. However, foreign issuers may wish to publish related press releases before EDGAR's

[2] Source: SEC No-Action Letter (23 January 2015), https://www.sec.gov/divisions/corpfin/cf-noaction/2015/abbreviated-offers-debt-securities012315-sec14.pdf.

As a technical matter, the best price rule does not apply to debt securities and only to tender offers for equity securities. However, it is followed in practice in US debt tender offers and practitioners generally take the view that US holders must be excluded from a true Dutch Auction debt tender.

Alternatively, issuers may use a "Modified Reverse Dutch Auction", which invites bondholders to submit bids specifying the price at which they are willing to tender, within a predetermined price range. The issuer ranks bids from the lowest price upward, accepting offers until the desired and pre-set amount of bonds is repurchased, with all accepted bids settling at the clearing price (set at the highest accepted bid). The SEC has confirmed that this structure is compliant with the US tender offer rules subject to compliance with certain conditions, including: (1) disclosure in the tender offer materials of the minimum and maximum consideration to be paid; (2) pro rata acceptance throughout the offer with all securities purchased participating equally in prorationing; (3) withdrawal rights throughout the offer; (4) prompt announcement of the purchase price, if determined prior to the expiration of the offer; and (5) purchase of all accepted securities at the highest price paid to any security holder under the offer.

Liability Management by Sovereigns

Pursuant to Rule 3a12-3(a) under the Exchange Act, foreign governments or political subdivisions thereof that are eligible to file registration statements on Form 18 with the SEC are exempt from Section 14 of the Exchange Act and the tender offer rules thereunder. It is worth noting that the sovereign bonds targeted in a tender offer do not need to be registered on Form 18 to be exempt from the application of the US tender offer rules and it is sufficient that the issuer is eligible to use Form 18 in respect of such securities. As a result, sovereign bonds are exempt from the US tender offer rules even if they were issued in a Rule 144A/Regulation S offering.

As sovereign issuers need not comply with Rule 14e-1or the best price rule, they have greater flexibility in structuring liability management transactions and can minimise market risk by executing tender offers on a very short timetable. However, even if a sovereign tender offer is exempt from US tender offer rules, it will remain subject to the antifraud provisions of Section 10(b) of the Exchange Act and Rule 10b-5 thereunder.

Switch Tender Offers

In recent years, sovereign issuers have taken advantage of their exemption from US tender offer rules to execute an innovative liability management transaction known as the "switch" tender offer, which combines a tender offer with an issue of new bonds. A switch tender offer is structured to provide bondholders with the option to (a) tender the bonds for cash (sometimes called the "non-preferred tender") or (b) tender the bonds with a concurrent "indication of interest" (i.e. a firm bid) to purchase the equivalent principal amount of the new bonds (the preferred tender). In practice, issuers rarely accept non-preferred tenders for cash and only accept tenders with concurrent indications of interest to purchase new bonds.

The switch tender offer transaction first emerged in 2012 and has been adopted by many sovereigns since then as it allows the issuer to exchange the existing bonds and raise additional funds through the new issuance with a single billing and delivery bank settling both the tender offer and the new issuance. Switch tender offers are typically executed intra-day and are

conditioned on the successful pricing of the new bonds later that same day. This accelerated timeline minimises exposure to market volatility that may otherwise adversely impact a successful tender or exchange if left open for a longer period. It is important to note that the issuer will assume credit risk on the existing bonds for the period between the settlement of the tender offer and the issuance of the new bonds. Accordingly, it is important that the timing of the settlement of the tender offer and the new issue are aligned as closely as possible.

Conclusion

Liability management structures and the SEC's application of US tender offer rules have changed significantly in the past and will continue to evolve based on the needs of debt market participants. The variety of techniques and the potential for US laws and regulations to impact the process mean that an issuer should not embark upon a liability management transaction without first considering the issues described in this article. We would be happy to discuss these structures and techniques with any interested issuer.

CONTACTS

Jill Concannon
Partner, London

T +44 20 7006 1142
E jill.concannon@cliffordchance.com

Michael Dakin
Partner, London

T +44 20 7006 2856
E michael.dakin@cliffordchance.com

Johannes Juette
Partner, London

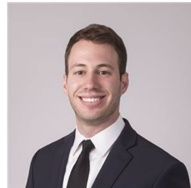
T +44 20 7006 5015
E johannes.juette@cliffordchance.com

Drew Rundus
Partner, London

T +44 20 7006 2875
E drew.rundus@cliffordchance.com

Alan Yeung
Partner, Hong Kong

T +852 2826 3520
E alan.yeung@cliffordchance.com

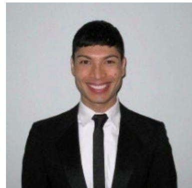


Jake Ducharme
Senior Associate, New York

T +1 212 878 4953
E jake.ducharme@cliffordchance.com

Yash Ranade
Senior Associate (US), London

T ++44 20 7006 1458
E yash.ranade@cliffordchance.com



Sannu Shrestha
Senior Associate (US), London

T +44 20 7006 3396
E sannu.shrestha@cliffordchance.com

Sarah Wetzel
Associate (US), London

T +44 20 7006 1154
E sarah.wetzel@cliffordchance.com

Rebecca Hoskins
Professional Support Lawyer, New York

T +1 212 878 3118
E rebecca.hoskins@cliffordchance.com

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www.cliffordchance.com

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