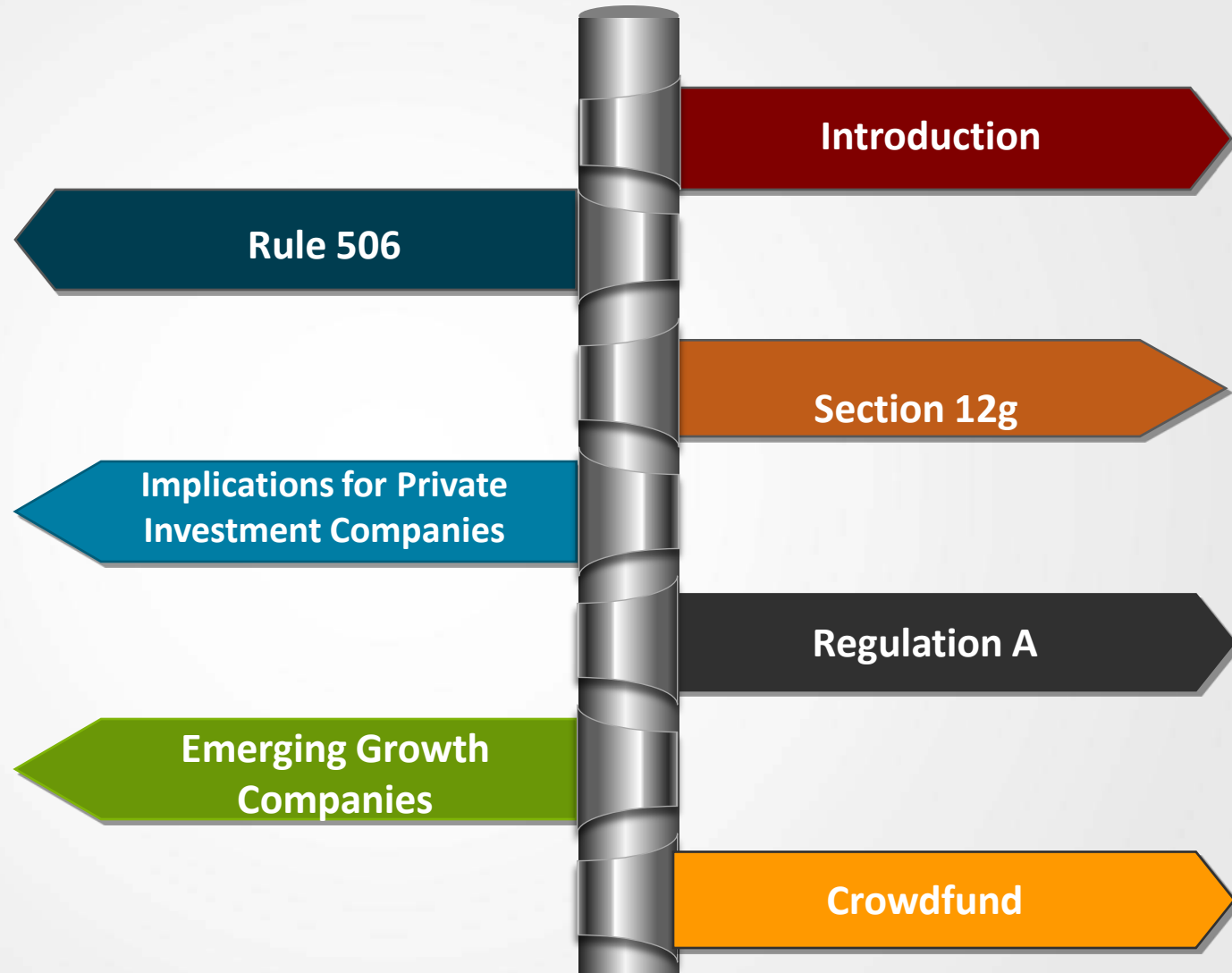


Jumpstart Our Business Startups ("JOBS") Act

OSB Securities Law Section
Portland, OR
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Sub- topics



Panelists



Christopher Hall



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Rule 506

Access to Capital for Job Creators

Rule 506

Current Rule 506 of Regulation D

- › Widely relied upon exemption from registration by private and small reporting companies
 - › Unlimited number of accredited investors (and up to 35 non-accredited investors, if specific information is delivered prior to purchase)
 - › No dollar limit on the amount of money an issuer can raise
 - › Securities sold are exempt from state registration and qualification provisions
 - › No specific form of disclosure required if sales are made only to accredited investors
- › No use of general solicitation or advertising in making offers and sales of securities = pre-existing substantive business relationship between issuer and potential investors

Rule 506

Public Solicitation in Certain Private Offerings

Removes the prohibition on general solicitation and advertising in Rule 506 private placements in which **ALL PURCHASERS** are "**accredited investors**"

Requires companies to take reasonable steps to determine each purchaser's accredited status, using methods determined by the SEC

Directs the SEC to implement these changes by July 4, 2012

Rule 506

Creation of Rule 506 Trading Platforms

Exempts certain market participants in Rule 506 offerings from registering as a broker-dealer solely because they:

- › Maintain Internet sites and other platforms permitting offers, sales, purchases, negotiations, general solicitation or similar activities by issuers of the securities;
- › Co-invest in the securities; and/or
- › Provide ancillary services, including certain due diligence and standardized documentation services, related to the securities

Rule 506

Broker-Dealer Exemption - Limitations

- › To qualify for the exemption, such person or any person associated with such person:
 - › *Cannot* receive compensation in connection with the purchase or sale of such securities;
 - › *Cannot* have possession of customer funds or the securities; and
 - › *Cannot* be subject to a statutory disqualification (e.g., expelled or suspended from membership or participation in a stock exchange)

Rule 506

Practical Effect

- › Could *radically* change the way private companies and funds communicate with investors and raise capital
 - › Use of Web and social media
 - › Potential for broad-based advertisement in print, TV and other media
- › Remains to be seen what SEC rules in fact will permit

Rule 506

Practical Effect

- › Compliance with technical requirements of Rule 506 will be critical (e.g., timely filings of Form D, accredited investor status of purchasers, integration of multiple offerings)
 - › *Important:* The JOBS Act does NOT change the ban on general solicitation in private placements conducted outside of Rule 506
 - › There is NO fallback exemption for a "blown" Rule 506 offering in which there has been public solicitation or advertising.

Rule 506

Practical Effect

Increased SEC scrutiny of accredited investor status in Rule 506 offerings with general solicitation

Companies will need to decide whether public advertising is worth giving up sophisticated purchasers who are not accredited investors. Potential factors:

- › Extent of competition for accredited investors
- › Nature of SEC restrictions on "advertising"
- › Effectiveness of trading platforms that develop (which may depend on SEC guidance on "no compensation" restriction in broker-dealer exemption)

Rule 506

Be Mindful

- Securities sold under Rule 506 are restricted securities
- Antifraud provisions of federal securities laws continue to apply
- The Rule 506 changes are not self-effectuating and require rulemaking by the SEC

Rule 506

At Present...

The current requirements remain in effect (i.e., no advertising or public solicitation)

Continue to follow customary procedures for Rule 506 transactions

SEC is taking comments on its Website: www.sec.gov

12g Registration Threshold

Title V: Private Company Flexibility and Growth

Title VI: Capital Expansion

12(g) Registration Threshold

Increase in Holders of Record Threshold to 2,000 Persons

The JOBS Act increases the "holders of record" threshold at which a company must register under the Exchange Act

- › From 500 to 2,000 persons
- › Provided fewer than 500 persons are not accredited investors

Total assets threshold of \$10m remains unchanged

Deregistration threshold remains the same

- › Less than 300 holders of record (500 if assets less than \$10m in last 3 years, except for bank holding companies is 1,200)

12(g) Registration Threshold

Exclusions from Definition of Holders of Record

Securities "held of record" excludes

- › Securities held by a person who received them in exempt transactions through an employee compensation plan
 - › Effective immediately, but SEC is directed to adopt safe harbor provisions
 - › Based on legislative history exemption should be construed broadly
- › Also excludes securities issued in crowdfunding transactions
 - › Effective only after SEC rulemaking

12(g) Registration Threshold

Exchange Act Relief for Equity Compensation Plans

- › Exclusion from holders of record definition extends existing limited 12(g) relief for options and RSUs
 - › Which required restrictions on transfer, exemption under Rule 701
- › New relief should apply to all forms of equity-based compensation
 - › Including restricted stock and SARs
- › New relief should apply to all forms of exemption traditionally relied on for grants to U.S. and foreign employees
 - › Rule 701, Regulation D, Regulation S, Section 4(2), "no sale" theory

12(g) Registration Threshold

What does this mean?

Increased flexibility of private companies in granting equity compensation as the number of employees increases

- › Still must review compliance with Securities Act exemptions and applicable state and foreign securities laws, including disclosure requirements

Increased ability of companies to stay private longer and utilize some of the other capital raising provisions contemplated in the Act or otherwise available to them

Implications for Private Investment Companies

Private Investment Companies

1940 Act Exemptions

Section 3(c)(1)

➤ Any issuer (i) whose outstanding securities (other than short-term paper) are beneficially owned by no more than 100 persons, and (ii) is not making and does not presently propose to make a public offering of its securities

Section 3(c)(7)

➤ Any issuer the outstanding securities of which are owned exclusively by persons who, at the time of acquisition of such securities, are qualified purchasers, and which is not making and does not at that time propose to make a public offering of such securities

Private Investment Companies

Intersection of Securities Act and 1940 Act

Concept of "public offering" in the 1940 Act and the Securities Act

- Traditionally co-terminus
- New definition could liberalize what a "public offering" means for 1940 Act purposes for private equity and hedge funds

Elevated threshold under 12(g)

- Effectively increases the number of potential shareholders in a Section 3(c)(7) fund from 500 to 2,000

Regulation A+

Regulation A+

Small Company Capital Formation

Background: Regulation A

- › Securities Act Section 3(b) permits offerings of up to \$5 million (includes up to \$1.5 million in resales by existing security holders)
- › Securities are not "covered securities" and are therefore subject to state blue sky laws
- › Offering document filed with and qualified by SEC
 - › **May contain unaudited financial statements**
 - › **Reduced disclosure requirements**
 - › **No ongoing Exchange Act reporting obligations**

Regulation A+

Small Company Capital Formation

"Regulation A+" – A Supercharged Regulation A

- › Section 3(b): expanded by JOBS Act to authorize "unregistered" public offerings of up to \$50 million through a "mini-registration" process similar to Regulation A
- › Features of Regulation A+:
 - › Securities may be offered publicly
 - › Securities will not be "restricted"
 - › No investor qualification standards (with caveats)
 - › Can be used in underwritten offerings or DPOs
 - › Issuers can "test the waters" before filing offering statement

Regulation A+

Small Company Capital Formation

Blue Sky Preemption Under Regulation A+

- "Blue sky" preemption: JOBS Act contemplates that securities offered under "Regulation A+" will not be subject to state "blue sky" regulation if:

- Offered/sold on a national securities exchange (e.g., NYSE or Nasdaq), or

- Offered/sold to "qualified purchasers" – to be defined by SEC rule

Regulation A+

Small Company Capital Formation

"Regulation A+" – SEC Rulemaking

Implementation of "Regulation A+" dependent on SEC rulemaking

- › SEC regulations mandated by JOBS Act but no specific timetable
- › SEC authorized to adopt rules "necessary . . . for the protection of investors" including:
 - › Filing of offering statement with SEC and distribution of offering statement to prospective investors
 - › To include a description of issuer's business, financial condition, governance principals, use of funds and "other appropriate information"
 - › Audited financial statements will be required (though number of years not specified in JOBS Act)

Regulation A+

Small Company Capital Formation

"Regulation A+" – SEC Rulemaking

- › "Testing the waters" – ability of issuers to solicit interest in the offering prior to filing of offering statement also to be defined by SEC rulemaking
- › Periodic Reporting:
 - › SEC rules must require "Regulation A+" issuers to file audited financial statements with SEC on annual basis
 - › No other periodic reporting mandated, but SEC authorized to adopt rules requiring "Regulation A+" issuers to file "periodic disclosures" with SEC
- › Disqualification provisions: "Regulation A+" exemption to be unavailable if issuer, affiliates, officers/directors and/or underwriters are "disqualified" under rules to be adopted by SEC

IPO On-Ramp

Emerging Growth Companies

IPO On-Ramp

Emerging Growth Companies

How does the JOBS Act define an Emerging Growth Company?

- › A company with annual gross revenues of less than \$1 billion during most recently completed fiscal year.
- › A company will remain an EGC until the earliest of:
 - › Last day of the fiscal year in which its revenues are \geq \$1 billion
 - › Last day of the fiscal year following the fifth anniversary of the date of first sale of common equity registered under the Securities Act
 - › Date on which it has, during the previous 3-year period, issued $>$ \$1 billion in non-convertible debt
 - › Date on which it is deemed to be a ‘large accelerated filer’

IPO On-Ramp

Emerging Growth Companies

DECEMBER 2011						
Sun	Mon	Tues	Wed	Thurs	Fri	Sat
				1	2	3
4	5	6	7	8	9	10
11	12	13	14	15	16	17
18	19	20	21	22	23	24
25	26	27	28	29	30	31

IPO On or Prior to

12.8.2011...

NOT

an Emerging Growth Company

IPO On-Ramp

Emerging Growth Companies

Reduced Disclosure Requirements

- › **Confidential S-1 submission**
 - › File at least 21 days prior to road show Need not present more than 2 years audited financials in IPO registration statement
- › **Financial Disclosure**
 - › 2 years of audited financials in IPO S-1
 - › Similar requirements for MD&A and selected financial information
- › **Executive compensation disclosure requirements significantly reduced**
 - › Fewer tables
 - › Fewer years
 - › Fewer executives covered

IPO On-Ramp

Emerging Growth Companies

Increased Communications with Investors

EGCs can test the waters

- › Oral or written communications with QIBs or institutional accredited investors before or after filing of S-1

Investment banks no longer subject to traditional quiet period(s) on publishing reports on EGCs

- › Can publish before offering/during/after offering

Relax restrictions on securities analyst communications

- › Securities analysts can participate in communications with management of EGC along with representatives broker/dealer

IPO On-Ramp

Emerging Growth Companies

Confidential Submissions

- › Only available prior to "initial public offering date"
- › Not available for Exchange Act submissions
- › Remains available for Foreign Private Issuers
- › Filing fee not payable upon submission – only pay when actually file

IPO On-Ramp

Emerging Growth Companies

Confidential Submissions

- › SEC will require substantially complete filing
 - › Not required to be signed
 - › No auditor/expert consents
 - › **Must include signed audit report**
 - › SEC expects exhibits to be included
- › Initial submission and amendments filed as Exhibits 99.x when actually file registration statement

IPO On-Ramp

Emerging Growth Companies

Reduced Reporting Requirements

- › EGCs are exempt from:
 - › Auditor attestation of the company's internal control over financial reporting
 - › Stockholder advisory vote on executive compensation
 - › Stockholder advisory vote on golden parachute compensation
 - › Disclosing relationship between executive compensation paid and company financial performance
- › Delayed Compliance with new financial accounting standards

IPO On-Ramp

Emerging Growth Companies

More Changes to Come

- › SEC must conduct several studies/reports including:
 - › Impact of decimalization on liquidity for small and medium cap companies (90 days)
 - › Updating registration requirements to simplify the process and reduce related costs and burdens on EGCs, including potential amendments to Reg S-K (report due by October 5, 2012)

Crowdfund

Crowdfund

Provisions

C
R
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N
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Capital
Raising
Online
While
Deterring
Fraud and
Unethical
Non-
Disclosure Act

Crowdfund

Provisions

- › New Section 4(6) offering exemption
- › Non-reporting issuers only
- › Raise up to \$1 million in 12-month period
- › Maximum investment limits per investor
 - › (aggregate ALL Crowdfund sales by issuer to investor in 12-month period)

Crowdfund

Transaction Requirements

- › Must be conducted through "intermediary"-broker or "funding portal"
- › No advertising – but can direct investors to broker or portal
- › May not compensate anyone to promote offering through channels provided by broker/funding portal unless take steps to ensure compensation disclosed
- › Comply with information requirements
- › Comply with other SEC rules (TBD)

Crowdfund

Transaction Information Requirements

- › Specified info of issuer must be filed with SEC and provided to investors and intermediary
- › Name, legal status, physical address and website address of issuer
- › Names of directors and officers (and functional =)
- › Names of any 20+% stockholders
- › Description of issuer's business and issuer's anticipated business plan

Crowdfund

Transaction Information Requirements

Issuer's financial condition – information depends on 4(6) target offering amounts in preceding 12-month period:

- › ≤\$100K
 - › Income tax returns for most recently completed fiscal year
 - › Financial statements of issuer, certified by principal exec. officer as true and complete in all material respects
- › >\$100K to \$500K:
 - › Financial statements reviewed by independent public accountants (using standards and procedures established by SEC)
- › >\$500K (or such other limit set by SEC)
 - › Audited financial statements

Crowdfund

Transaction Information Requirements

- › Target offering amount
- › Deadline to reach target + regular updates
- › Price of securities or method for determining price
- › Purpose and intended use of proceeds

Crowdfund

Transaction Information Requirements

Ownership and capital structure of issuer

- › Terms of securities offered and other issuer classes; summary of differences
- › Description of impact of exercise of rights by issuer's principal stockholders on offered securities
- › Names and ownership levels of 20+% stockholders
- › How offered securities valued, and examples of how valued in future

Crowdfund

Transaction Information Requirements

- › Risks of ownership and corporate actions (e.g., additional stock issuances, sale of company, or transactions with related parties)
- › Annual (at least) reports of operations and financial statements (as determined by SEC) – filed with SEC and provided to investors
- › Compliance with other SEC rules as prescribed

Crowdfund

Broker/Funding Portal Requirements

- › Defined as "any person acting as an intermediary" in 4(6) transaction. Such person must:
- › Register with SEC as broker/funding portal
- › Register with applicable SRO
- › Provide SEC mandated disclosures to investors (risk and investor education)

Crowdfund

Broker/Funding Portal Requirements

- › Ensure investor review, affirmation and understanding regarding investment
- › Take SEC mandated actions to reduce fraud risk (including background check of directors, officers and 20+% stockholders)
- › Make available to SEC and investors information to be provided by issuer to investors and intermediaries
 - › At least 21 days prior to any sale
- › Take SEC determined actions to ensure that investors not exceeding 12-month investment limits

Crowdfund

Additional Transaction Considerations

- › Civil liability to purchasers for material misstatements or omissions
- › Securities treated as "covered securities"
- › Securities to be exempt from 12(g) count
- › Securities issued in transaction restricted from transfer for one year with certain exceptions

Crowdfund

Additional Transaction Considerations

Integrated with other offerings

Issuers



Includes:

- › Director or Partner
- › Principal Executive
- › Financial and Accounting Officers
- › Anyone offering or selling 4(6) security



270

Number of days the SEC
has to implement rules

JOBS Act

Rulemaking and Effectiveness

Provision	Effectiveness
➤ Confidential submission of draft registration statements by EGCs	Immediately
➤ Increased shareholder thresholds for public company reporting under Section 12(g)	Immediately
➤ Elimination of prohibitions on general solicitation and advertising	Requires implementation rules to be issued by the SEC by July 4, 2012; SEC has postponed to August 22, 2012 meeting
➤ Crowdfunding	Requires implementation rules to be issued by the SEC by December 31, 2013
➤ New Section 3(b)(2) exemption known as "Regulation A+"	Requires implementation rules to be issued by the SEC; no deadline established

Q & A