

The New Dynamic: Exempt Securities Offerings in the United States and Resales of Restricted Securities

February 24, 2016

Agenda

- Staying private longer
- Proliferation of exempt offering alternatives
 - Section 4(a)(2)
 - Rule 506
 - Regulation A
 - Regulation Crowdfunding
 - Proposed amendments to intrastate exemptions
- Resales of restricted securities
 - The new Section 4(a)(7) exemption

Overview

The JOBS Act and private offerings

- Although the aspect of the JOBS Act that has received the most attention relates to changes to the IPO process, in large measure, the JOBS Act related changes affecting the private market may be more significant.
 - Title V and Title VI changes to the Exchange Act Section 12(g) threshold
 - Changes to Rule 506
 - Legal certainty for matchmaking platforms
- Taken together, these measures have the effect of permitting companies to stay private longer and to rely on exempt offerings (while enabling companies to contact a broader range of potential investors) for their capital-raising.

Reliance on private or exempt offerings

- Even pre-JOBS Act, based on various studies, it was already the case that more capital was being raised in reliance on Regulation D and Rule 144A (in aggregate) than in SEC-registered offerings—according to the SEC’s Division of Economic Research and Analysis (DERA), in 2014, for example, the total raised in registered offerings was \$1.35 trillion whereas the total raised through all private offerings was more than \$2.0 trillion
 - Amounts for private offerings are likely to be understated given that many issuers fail to file Form Ds and amounts raised in 4(a)(2) offerings are not reported
 - The amounts raised in registered offerings include debt offerings, whereas the majority of Reg D offerings involve equity or “new capital”
- These trends are likely to have become more pronounced since 2014

Reliance on private or exempt offerings (cont'd)

- Many companies that were able to deregister following the JOBS Act have done so
 - Since the JOBS Act, approximately 90 banks have deregistered
 - These banks will now have to rely on private or exempt offerings in order to raise capital going forward
- Companies are choosing to defer their IPOs and rely on private financing for much longer than in the past
 - This is evident from various IPO reports
 - For example, based on statistics for the period from 1/1/12 through 9/30/15, the median market cap for IPO issuers was approximately \$386 million, and the average was \$1.4 billion
 - Fewer than 2.5% of IPO issuers have a market cap of \$50 million or less

Venture-backed companies delaying IPOs

- CB Insights reports that in 2015 global private companies raised \$90 billion from investors (an increase of 26% over 2014)
- Looking at the tech sector, U.S. venture-backed tech companies have raised more capital in the private market (\$51 billion) than the public market (\$6 billion) in 2015 (*CB Insights*)
- The number of tech IPOs in 2015 declined to 22
- October 19 *Wall Street Journal* headline: Tech Startups Feel an IPO Chill

Recent high profile pre-IPO private placements

 **Palantir**
\$500M

 **airbnb**
\$1.5B

 **Spotify**
\$526M

SPACEX
\$1.0B

Pinterest
\$367M


Snapchat
\$537M


UBER
\$2.8B

\$350M
 **Dropbox**

FanDuel
\$275M


\$300M

Rationale

- There may be a variety of different motivations for a late stage or pre-IPO private placement
 - Company may want to defer IPO and need to raise additional capital prior to the IPO
 - Company may want to take out early friends and family and angel investors and “clean up” balance sheet or provide partial liquidity for longstanding holders
 - Company may want to bring in strategic investors
 - Company may be advised that it should prepare itself for the IPO by gaining support and validation from key sector investors that are opinion leaders
 - Company and bankers may want to “de-risk” IPO by bringing in cross-over investors that will also invest in the IPO
 - Company may be advised that an up round will make higher IPO pricing easier for IPO investors to accept
 - May be quite sector dependent

Proliferation of Exempt Offering Alternatives

Section 4(a)(2)

- Transactional exemption
- Issuer exemption
 - Most utilized exemption
 - Application of the private placement exemption, however, has been the subject of significant debate due in large part to the brevity of its wording
 - Not a “public offering” has been defined by case law and SEC interpretation and one may look to safe harbors as well
- Restricted securities – securities sold in a private placement may not be resold absent registration or exemption from registration

Section 4(a)(2) (cont'd)

SEC v. Ralston Purina Co., 346 U.S. 119 (1953)

- Supreme Court confirmed SEC position that offers and sales to a large number of employees by Ralston Purina under its stock plan were not exempt under Section 4(a)(2); provided the following “guidance:”
 - §4(a)(2) exemption focuses on “offerees” and not actual purchasers of the securities.
 - § 4(a)(2) exemption does not depend upon a numerical test; Court rejected SEC argument that extensive number of offerees was sufficient by itself to establish loss of exemption.
 - Availability of §4(a)(2) exemption “*should turn on whether the particular class of persons...need the protection of the [’33] Act*” and whether the offerees “*are shown to be able to fend for themselves.*”
 - Court stated that where offerees do not have “access to the kind of information” that a registration statement would disclose, issuer required to provide same kind of information that otherwise generally would be available in a registration statement.

Section 4(a)(2) (cont'd)

- **Amount of offering:** amount is unlimited
- **By?** any issuer, whether reporting or non-reporting, can rely on Section 4(a)(2)
- **Who can invest?** sophisticated investors who can fend for themselves
- **What is the investor cap?** no applicable cap
- **Is an intermediary required?** effectively, yes, given that the issuer cannot use general solicitation or general advertising; issuer could raise capital from investors with whom it has a pre-existing substantive relationship
- **Manner of offering:** the offering cannot involve general solicitation or general advertising
- **Offering disclosure requirements:** none
- **Reporting following the offering:** none; no requirement to file a Form D
- **Transfer restrictions:** securities will be restricted securities

Section 4(a)(2) (cont'd)

- **Bad actor disqualification:** the disqualification is not applicable to Section 4(a)(2) offerings
- **Manner of offering:** generally, a Section 4(a)(2) offering will involve a placement agent; the placement agent will identify investors. Investors will conduct their own diligence review
- **Documentation:** there may or may not be an offering memorandum; the investors will sign a securities purchase agreement with the issuer; each investor will make payment to the issuer directly generally
- **State blue sky:** the securities are not “covered securities” however given offerings are limited to accredited investors or institutional accredited investors, typically state exemptions will be available

Rule 506 safe harbor

- Rule 506 is the most widely used exemptive rule under Regulation D, accounting for the overwhelming majority of capital raised under Regulation D.
- Traditional requirements of a Rule 506 private placement include:
 - No dollar limit on size of transaction.
 - Unlimited number of accredited investors and no more than 35 unaccredited investors.
 - No general solicitation or advertising (*now prohibition against general solicitation has been eliminated for 506(c) offerings*).
 - Resale limitations.
 - Disclosure required for non-accredited investors.
 - Form D filing within 15 days of first sale of securities.
 - Good faith effort to comply (Rule 508).

Rule 506(b)

- “Traditional” Rule 506 offering
- **Amount of offering:** unlimited
- **By?** Rule 506(b) can be used by reporting and non-reporting issuers, so long as issuer and other covered persons are not subject to bad actor disqualification
- **Who can invest?** Accredited investors and a limited number of non-accredited investors; in practice, offerings are limited to accredited investors
- **What is the investor cap?** None.
- **Is an intermediary required?** Not technically required; however, given that the issuer cannot use general solicitation or general advertising; issuer could raise capital from investors with whom it has a pre-existing substantive relationship
- **Manner of offering:** the offering cannot involve general solicitation
- **Reporting following the offering:** filing of a Form D

Rule 506(b) (cont'd)

- **Bad actor disqualification:** the issuer will be required to obtain information from all covered persons
- **Documentation:** there may or may not be an offering memorandum; the investors will sign a securities purchase agreement with the issuer; each investor will make payment to the issuer directly generally
- **State blue sky:** securities sold pursuant to Rule 506(b) are “covered securities”

“Accredited investor crowdfunding”

- Many “matchmaking portals” rely on Rule 506(b) to conduct internet-based offerings solely to accredited investors
- These offerings are structured such that the matchmaking portal makes an offer only to accredited investors with which the portal has established or has a pre-existing substantive relationship
- Issuer specific or offering specific information is not generally available and is made available only to “members” or on a password-protected basis to those investors known to the portal
- An accredited investor crowdfunded offering relies on the guidance provided in pre-JOBS Act no-action letters (*IPONet*, *Lamp Technologies*, etc.) and affirmed recently in C&DIs on general solicitation, as well as in a recently issued no-action letter, *CitizensVC*

Rule 506(c)

- Rule 506(c) permits the use of general solicitation, subject to the following conditions:
 - The issuer must take reasonable steps to verify that the purchasers of the securities are accredited investors;
 - All purchasers of securities must be accredited investors, either because they come within one of the enumerated categories of persons that qualify as accredited investors or the issuer reasonably believes that they qualify as accredited investors, at the time of the sale of the securities; and
 - The conditions of Rule 501 and Rules 502(a) and 502(d) are satisfied

Rule 506(c) (cont'd)

- Reasonable steps to verify investor status
- Principles-based guidance includes a list of factors to consider:
 - *The nature of the purchaser.* The SEC describes the different types of accredited investors, including broker-dealers, investment companies or business development companies, employee benefit plans, and wealthy individuals and charities
 - *The nature and amount of information about the purchaser.* Simply put, the SEC states that “the more information an issuer has indicating that a prospective purchaser is an accredited investor, the fewer steps it would have to take, and vice versa”
 - *The nature of the offering.* The nature of the offering may be relevant in determining the reasonableness of steps taken to verify status, *i.e.*, issuers may be required to take additional verification steps to the extent that solicitations are made broadly, such as through a website accessible to the general public, or through the use of social media or email

Rule 506(c) (cont'd)

- Final rule does not provide for a safe harbor; however, it does set out a supplemental non-exclusive list of methods that may be used to satisfy the verification requirement, including:
 - A review of IRS forms for the two most recent years and a written representation regarding the individual's expectation of attaining the necessary income level for the current year;
 - A review of bank statements, brokerage statements, tax assessments, etc. to assess assets, and a consumer report or credit report from at least one consumer reporting agency to assess liabilities;
 - A written confirmation from a registered broker-dealer, RIA, CPA, etc.
 - For existing investors (pre-506(c) effective date), a certification

Rule 506(c) (cont'd)

- **Amount of offering:** unlimited
- **By?** Rule 506(c) can be used by reporting and non-reporting issuers, so long as issuer and other covered persons are not subject to bad actor disqualification
- **Who can invest?** Accredited investors only
- **What is the investor cap?** None
- **Is an intermediary required?** Not technically required; easier for an issuer to conduct a Rule 506(c) offering on its own
- **Manner of offering:** involves general solicitation
- **Reporting following the offering:** filing of a Form D
- **Bad actor disqualification:** the issuer will be required to obtain information from all covered persons
- **Documentation:** there may or may not be an offering memorandum; the investors will sign a securities purchase agreement with the issuer; each investor will make payment to the issuer directly generally
- **State blue sky:** securities sold pursuant to Rule 506(b) are “covered securities”

Regulation A

- The SEC adopted final rules which:
 - Amend and modernize existing Regulation A.
 - Create two tiers of offerings:
 - Tier 1 for offerings of up to \$20m (\$6m for selling stockholders); or
 - Tier 2 for offerings of up to \$50m (\$15m for selling stockholders).
 - Set issuer eligibility, disclosure and reporting requirements.
 - Impose additional disclosure and ongoing reporting requirements, as well as an investment limit, for Tier 2 offerings, and, given these investor protection measures, makes Tier 2 offerings exempt from certain blue sky requirements.
 - Became effective June 19, 2015

Regulation A (cont'd)

- **Amount of offering:** Tier 1 up to \$20 million in 12-month period, Tier 2 up to \$50 million in 12-month period
- **By?** Eligible issuers are non-reporting issuers, organized in and with their principal place of business in the United States or Canada, other than funds, blank check companies, issuers subject to various disqualifications
- **Who can invest?** Accredited and non-accredited investors
- **What is the investor cap?** A non-accredited natural person is subject to an investment limit and must limit purchases to no more than 10% of the greater of the investor's annual income and net worth, determined as provided in Rule 501 of Regulation D (for non-accredited, non-natural persons, the 10% limit is based on annual revenues and net assets). The investment limit does not apply to accredited investors and will not apply if the securities are to be listed on a national securities exchange at the consummation of the offering
- **Is an intermediary required?** No
- **Manner of offering:** the offering may involve "testing the waters"

Regulation A (cont'd)

- **Offering disclosure requirements:** an issuer must prepare and file with the SEC and have qualified an offering statement on Form 1-A.
- Part I (Notification) requires certain basic information regarding the issuer, its eligibility, the offering details, the jurisdictions where the securities will be offered, and sales of unregistered securities.
- Part II (Offering Circular)
 - Part II contains the narrative portion of the Offering Circular and requires disclosures of basic information about the issuer; material risks; use of proceeds; an overview of the issuer's business; an MD&A type discussion; disclosures about executive officers and directors and compensation; beneficial ownership information; related party transactions; and a description of the offered securities.
 - This is similar to Part I of Form S-1 and an issuer can choose to comply with Part I of Form S-1 in connection with its Offering Circular.
 - An issuer that chooses to list its securities concurrent with the completion of a Regulation A offering will be required to use Part I of Form S-1 in connection with the Offering Circular
 - Other Tier 2 issuers also are likely to use Part I of Form S-1 as well

Regulation A (cont'd)

- **Financial statement requirements:** differ for Tier 1 and Tier 2 offerings:
 - Tier 1 and Tier 2 issuers must file balance sheets and other required financial statements as of the two most recently completed fiscal year ends, or for such shorter time as they have been in existence, subject to certain exceptions.
 - The financial statements for an issuer in a Tier 2 offering are required to be audited by an independent auditor that need not be PCAOB-registered, except as noted below.
 - An issuer in a Tier 2 offering that seeks to have a class of securities listed on a national securities exchange concurrent with the Regulation A offering must include financial statements audited in accordance with PCAOB standards by a PCAOB-registered firm.
- **Advertising:** an issuer may solicit any investors (not subject to the requirements applicable to EGCs, for example); materials may be used both before and after the offering statement is filed
- **Intermediary restrictions and requirements:** an issuer can conduct a Regulation A offering with or without a financial intermediary

Regulation A (cont'd)

- **Reporting following the offering:** Tier 1 issuers would have no ongoing reporting obligation, other than to file an exit report on Form 1-Z within 30 days after the termination or completion of a Regulation A-exempt offering. Tier 2 issuers will be subject to ongoing reporting. Tier 2 issuers would be required to file:
 - Annual reports on Form 1-K (120 calendar days after the issuer's fiscal year end);
 - Semi-annual reports on Form 1-SA (90 calendar days after the end of the first six months of the issuer's fiscal year);
 - Current reports on Form 1-U;
 - Special financial reports on Form 1-K and Form 1-SA; and
 - Exit reports on Form 1-Z.
- **Bad actor disqualification:** the issuer will be required to obtain information from all covered persons
- **State blue sky:** securities sold pursuant to Tier 1 will be subject to state blue sky requirements; securities sold pursuant to Tier 2 will be "covered securities"
- **Transfer restrictions:** securities sold pursuant to Regulation A are not "restricted securities"

Regulation Crowdfunding

- **Amount of offering:** up to \$1 million in a 12-month period through crowdfunding
- **By?** Issuers that are not reporting companies, not funds, and not subject to disqualification
- **Who can invest?** Accredited and non-accredited investors
- **Is there an investor cap?** An investor is subject to an investment limit on amounts invested in any 12-month period through crowdfunding equal to:
 - The greater of: \$2,000 or 5% of the lesser of the investor's annual income or net worth if either annual income or net worth is less than \$100,000; or
 - 10% of the lesser of the investor's annual income or net worth, not to exceed an amount sold of \$100,000, if both annual income and net worth are \$100,000 or more
- **Is an intermediary required?** Yes. An issuer can only engage in crowdfunding through a broker-dealer or a funding portal, and can use only one intermediary for an offering
- **Manner of offering:** the offering must be conducted only through the platform

Regulation Crowdfunding (cont'd)

- **Offering disclosure requirements:** an issuer that elects to engage in a crowdfunded offering will be required to prepare initial disclosure about the issuer and the offering on Form C
- Form C requirements resemble the Form 1-A requirements for a Regulation A offering and include a discussion of:
 - Use of Proceeds;
 - The Targeted Offering Size;
 - Offering Price;
 - Business;
 - Directors and officers;
 - Beneficial Ownership and Capital Structure;
 - Indebtedness;
 - Related party transactions;
 - Exempt offerings;
 - Risk factors;
 - Transfer restrictions; and
 - Management's Discussion and Analysis.

Regulation Crowdfunding (cont'd)

- **Financial Statement Requirements:** in addition, a Form C must include certain financial statements prepared in accordance with U.S. GAAP. Audited financial statements must be conducted in accordance either with AICPA standards or PCAOB standards. Requirements depend on the target offering size as follows:
 - **\$100,000 or less:** the amount of total income, taxable income and total tax or equivalent line items, as reported on the federal tax forms filed by the issuer for the most recently completed year (if any), certified by the principal executive officer of the issuer, and the financial statements of the issuer, also certified by the principal executive officer. If financial statements of the issuer are available that have either been reviewed or audited by a public accountant independent of the issuer, then, these financial statements must be provided instead of the materials described in the preceding sentence.
 - **More than \$100,000 and less than \$500,000:** financial statements of the issuer reviewed by a public accountant independent of the issuer. If financial statements of the issuer are available that have been audited by a public accountant independent of the issuer, the issuer must provide those instead of the reviewed statements.

Regulation Crowdfunding (cont'd)

- **More than \$500,000**: financial statements of the issuer audited by a public accountant independent of the issuer; provided, however, that for issuers that are first-time issuers, offerings that have a target offering amount of more than \$500,000 but not more than \$1 million, financial statements of the issuer reviewed by a public accountant independent of the issuer. If audited statements are available, those must be provided instead.

Regulation Crowdfunding (cont'd)

- **Advertising:** an issuer's ability to advertise or promote the offering is limited to certain offering notices (basic offering details) and certain communications with potential investors made through the platform
- **Intermediary restrictions and requirements:** the intermediary is subject to educational and other obligations and limitations
- **Reporting following the offering:** until an issuer terminates its reporting obligations, it is required to file amendments for material changes (C/A), periodic updates (C-U) and annual filings (C-AR)
- **Transfer restrictions:** securities sold in such an offering are subject to certain transfer restrictions for one year

Rule 147 and Rule 504 and Proposed Amendments

Rule 147

- Section 3(a) of the Securities Act provides an exemption from the registration requirements for “any security which is a part of an issue offered and sold only to persons resident within a single State or Territory, where the issuer of such security is a person resident and doing business within or, if a corporation, incorporated by and doing business within, such State or Territory.”
- Section 3(a)(11) provides an exemption provided that:
 - The issuer be incorporated (and resident) and doing business in the state; and
 - The securities are offered and sold to persons resident in the state.
- **Amount of offering:** no limitations on the dollar amount being raised
- **Who can invest:** no limitations on the number or the sophistication of offerees or purchasers
- **Advertising:** no publicity or general solicitation restrictions, except offers and sales may be made only to residents of one state
- **Disclosure requirements:** no specific disclosure requirements apart from the resale restrictions

Rule 147 (cont'd)

- Rule 147 is a safe harbor under Section 3(a)(11); if the conditions of the safe harbor have not been satisfied, the 3(a)(11) exemption may still be available.
- Conditions of safe harbor:
 - To be “doing business” in the state, the issuer must derive 80% of its consolidated gross revenues from the state, and have 80% of its consolidated assets located in the state, and use 80% of the net offering proceeds in the state, and have its principal office in the state;
 - The entire offering must be made under the exemption, i.e., no additional offers and sales of securities that would be integrated may be made under any other exemption from registration—integration is determined under the five factor test subject to the rule of thumb that offers and sales made more than 6 months before or after an intrastate offering will not be integrated; and
 - Resales of the securities within nine months of an intrastate offering may only be made to residents of the same state—and the securities must be legended, and transfer restrictions imposed, to reflect this resale restriction.

Proposed amendments to Rule 147

- Rule 147, as it is proposed to be amended, would no longer fall within the statutory parameters of Section 3(a)(11)
- Proposed changes are as follows:
 - Eliminate the restriction on offers; allow an issuer to engage in any form of general solicitation
 - Continue to require that sales be made only to residents of an issuer's state or territory, but add a reasonable belief standard to the issuer's determination of residence of purchaser
 - Would eliminate the current requirement in Rule 147 that issuers obtain a written representation from each purchaser as to his or her residence.
 - Limit availability of the exemption to offerings that are either registered in the state in which all of the purchasers are resident, or conducted pursuant to an exemption from state law registration in such state that limits the amount of securities an issuer may sell pursuant to such exemption to no more than \$5 million in a 12-month period and imposes an investment limitation on investors
 - An issuer that changes its principal place of business would not be able to rely on Rule 147 in the new state until such time as the securities sold in reliance on the proposed exemption in the prior state have come to rest in that state (9 months)
 - Proposes to align the integration safe harbor in Rule 147 with the recently-adopted integration safe harbor in Rule 251(c) of Regulation A

Proposed amendments to Rule 147

(cont'd)

- Determining an issuer's principal place of business:
 - An issuer's principal place of business would be defined as the location in which the officers, partners, or managers of the issuer primarily direct, control and coordinate the activities of the issuer
 - In addition to having its principal place of business in-state, the issuer must meet at least one of the following requirements (instead of all requirements as currently specified in Rule 147):
 - the issuer derived at least 80% of its consolidated gross revenues from the operation of a business or of real property located in or from the rendering of services within such state or territory;
 - the issuer had at the end of its most recent semi-annual fiscal period prior to the first offer of securities pursuant to the exemption, at least 80% of its consolidated assets located within such state or territory;
 - the issuer intends to use and uses at least 80% of the net proceeds to the issuer from sales made pursuant to the exemption in connection with the operation of a business or of real property, the purchase of real property located in, or the rendering of services within such state or territory; or
 - a majority of the issuer's employees are based in such state or territory (this fourth prong is proposed to be added to the list)

Current Rule 504

- An exemption pursuant to Section 3(b) of the Securities Act; Section 3(b) authorizes the SEC to exempt from the registration requirements of the Securities Act offerings of securities not exceeding \$5 million
- **Amount of offering:** \$1 million of securities sold under Rule 504 within a 12-month period, less selling price of other securities sold under another section 3(b) exemption within prior 12 months
- **By?** Issuer cannot be a reporting company, an investment company or a SPAC
- **Who can invest?** Depends on form of offering
- **Is there an investor cap?** No
- **Manner of offering:** a private placement or an offering registered under applicable state laws
 - If it is structured as a private placement, then the issuer cannot use general solicitation or general advertising and must obtain investment representations, impose transfer restrictions, use restrictive legends on the securities, etc.

Current Rule 504 (cont'd)

- If it is structured as a state-registered offering, the issuer must comply with state registration requirements (“qualification”) in each state where securities are sold, including preparing and delivering a required “substantive disclosure document before sale” to purchasers in all states (whether or not each state requires registration and delivery of a disclosure document), or sell only to “accredited investors” in accordance with available state law exemptions that permit general solicitation and general advertising
- **Is an intermediary required?** No, although it would be challenging for an issuer to complete a Rule 504 offering as a private placement on its own
- **Offering disclosure requirements:** as discussed above, these depend on the manner of offering
- **Reporting following the offering:** none
- **Form D:** issuer must file a Form D

Proposed amendments to Rule 504

- The SEC proposes to amend Rule 504:
 - To increase the aggregate amount of securities that may be offered and sold in any twelve-month period from \$1 million to \$5 million
 - To disqualify certain bad actors from participation in Rule 504 offerings by referencing the disqualification provisions of Rule 506 of Regulation D
- By amending Rule 504, the SEC believes that the proposed changes “would facilitate state efforts to increase the efficiencies associated with the registration of securities offerings in multiple jurisdictions through regional coordinated review programs”

Resales of Restricted Securities

Resales of restricted securities

- With increased reliance on private placements and exempt offerings, and the desire on the part of many companies to remain private longer, there is increased focus on liquidity opportunities, including the resale of restricted securities
 - Employees and consultants of privately held companies often receive substantial portions of their overall compensation in the form of stock-based compensation awards. Historically, the expectation was that within a five to seven year time horizon (from startup) a successful company would consider an IPO and that IPO would provide a liquidity opportunity. Similarly, early investors, including friends, family and angel investors, often have an expectation of liquidity within that same time period.
 - Privately held companies may want to facilitate liquidity opportunities for employees, consultants and early investors through organized private secondary markets
 - Similarly, late-stage investors may be interested in purchasing securities from selling stockholders in these privately held companies

Resales of restricted securities

- For public companies that engage in private placements, providing a path to liquidity also is important

Resales of restricted securities

- Every offer and sale (including resales) of securities in the United States must be registered with the Securities and Exchange Commission unless an exemption is available
 - Otherwise, offer or sale violates Section 5 of Securities Act of 1933 (“Securities Act”)
- Key exemptions for private placements and resales of securities include:
 - Section 4(a)(1) of Securities Act: Exempts transactions by persons other than issuers, affiliates, underwriters or dealers
 - Section 4(a)(2) of Securities Act (and Regulation D safe harbor): Exempts transactions by the issuer not involving any public offering
 - Section 4(a)(3) of Securities Act: Generally exempts transactions by a dealers not acting as underwriters
- Securities sold in a private offering are “restricted securities” that may not be resold freely in the U.S. public secondary market

Resales of restricted securities (cont'd)

- Restricted Securities: Securities acquired in unregistered, private sales from the issuer or from an affiliate of the issuer
- Control Securities: Securities held by an affiliate of the issuer
 - An “*affiliate*” of the issuer is a person controlling, controlled by or under common control with the issuer
 - “*Control*” means the power to direct the management and policies of the company in question, whether through the ownership of voting securities, by contract, or otherwise
 - Generally includes officers, directors and greater than 10% shareholders, but requires facts and circumstances analysis
- Sections 4(a)(1) and 4(a)(3) are not available for resales of restricted or control securities
- For resales of privately placed securities and securities held by an affiliate of the issuer, a holder needs to find other available exemptions for its resales or have its resales covered by a registration statement

Existing resale exemptions

- Resale exemptions include:
 - Rule 144: Non-exclusive safe harbor for public resale of restricted and control securities subject to compliance with certain conditions
 - “Section 4(a)(1½)”: Technique developed by bar to facilitate private resales similar to 4(a)(2) private placements
 - Rule 144A: Private resales to QIBs
 - Regulation S under Securities Act: Resales of securities in “offshore transactions” with no “directed selling efforts” in United States

Rule 144

- Rule 144 provides a non-exclusive safe harbor for public resales of restricted securities
 - Without the types of limitations imposed by the rule, investors in a private placement (and their transferees) may be deemed to be taking with a view to distribution, who would be unable to rely on Section 4(a)(1) or, in the case of dealers, Section 4(a)(3) of the Securities Act
 - Adopted in 1972, Rule 144 has been amended from time to time (most recently in December 2007), generally to make it easier for holders to take advantage of the rule
- If a holder satisfies all of Rule 144's applicable conditions, the holder is generally deemed not to be an "underwriter"
 - Conditions differ for affiliates and non-affiliates
 - Generally not available for business combination related shell companies or asset-backed issuers (1 year look-back)
- Securities sold pursuant to Rule 144 are no longer "restricted securities" and may be resold freely by non-affiliate purchasers of the securities

Rule 144 – Sales by Affiliates

- Minimum holding period
 - For restricted securities held by an affiliate: (1) 6 months if the issuer has been a reporting company for at least 90 days; or (2) 1 year for other issuers
 - If shares are just control securities and not restricted securities, no holding period would apply
- Current public information
 - For reporting issuers, filed all required periodic reports in the last 12 months
 - For non-reporting issuers, certain specified company information is publicly available
- Manner of sale
 - For debt securities (including non-participatory preferred stock and asset-backed securities), no manner of sale limitations
 - For equity securities, the securities must be sold on an unsolicited basis, and either in (1) “brokers’ transactions,” (2) transactions with a market-maker or (3) “riskless principal” transactions (subject to compliance with certain requirements)

Rule 144 – Sales by Affiliates (cont'd)

- Form 144 filing
 - If sales during any 3-month period exceeds 5,000 shares or a price of \$50,000, a notice must be filed with the SEC (and if listed, relevant securities exchange)
 - Must have bona fide intention to sell within a reasonable time (generally 3 months)
- Volume limitation
 - For *equity securities*, an affiliate's Rule 144 sales cannot exceed, in the preceding 3-month period, the greater of (1) 1% of the outstanding securities of the class and (2) the average weekly trading volume of the securities on relevant U.S. exchanges during the preceding four weeks
 - For *debt securities*, an affiliate's Rule 144 sales cannot exceed the greater of (1) limitations set by either of the two tests described above and (2) 10% of the principal amount of the tranche of debt securities in question (or class, when the securities are non-participatory preferred stock) in the preceding 3-month period

Rule 144 – Sales by Affiliates (cont'd)

- A “non-affiliate” is any person who is not an affiliate of the issuer at the time of sale and has not been an affiliate for at least 90 days prior to that time
- Minimum holding period
 - The same holding periods that apply to sales of restricted securities by affiliates also apply to sales by non-affiliates (*i.e.*, a 6-month holding period for securities of reporting companies and a 1-year holding period for securities of non-reporting companies)
- Current public information
 - During the period from 6 months to 1 year, non-affiliates may resell publicly securities of a reporting company so long as that company continues to make available the information required by Rule 144(c)
 - After one year, non-affiliates may resell publicly securities of both reporting companies and non-reporting companies
- No other Rule 144 conditions apply to sales by non-affiliates

Recap of Rule 144

	Affiliate or Person Selling on Behalf of an Affiliate	Non-Affiliate (and Has Not Been an Affiliate During the Prior Three Months)
Restricted Securities of Reporting Issuers	<p><u>During six-month holding period:</u> No resales under Rule 144 permitted.</p> <p><u>After six-month holding period:</u> May resell in accordance with all Rule 144 requirements including:</p> <ul style="list-style-type: none"> •Current public information; •Volume limitations; •Manner-of-sale requirements for equity securities; and •Filing of Form 144. 	<p><u>During six-month holding period:</u> No resales under Rule 144 permitted.</p> <p><u>After six-month holding period but before one year:</u> Unlimited public resales under Rule 144 except that the current public information requirement still applies.</p> <p><u>After one-year holding period:</u> Unlimited public resales under Rule 144; need not comply with any other Rule 144 requirements.</p>
Restricted Securities of Non-Reporting Issuers	<p><u>During one-year holding period:</u> No resales under Rule 144 permitted. After one-year holding period may resell in accordance with all Rule 144 requirements, including:</p> <ul style="list-style-type: none"> •Current public information; •Volume limitations; •Manner-of-sale requirements for equity securities; and •Filing of Form 144. 	<p><u>During one-year holding period:</u> No resales under Rule 144 permitted.</p> <p><u>After one-year holding period:</u> Unlimited public resales under Rule 144; need not comply with any other Rule 144 requirements.</p>
Unrestricted Securities	<p><u>No holding period:</u> May resell in accordance with all Rule 144 requirements, including:</p> <ul style="list-style-type: none"> •Current public information; •Volume limitations; •Manner-of-sale requirements for equity securities; and •Filing of Form 144. 	<p><u>No holding period:</u> Unlimited public resales under Section 4(a)(1) of the Securities Act. Former affiliates cannot freely resell securities for a period of 90-days after they cease to be affiliates.</p>

Private Resale Alternatives for Restricted Securities

An affiliate may not want, or may be unable, to comply with all of the conditions of Rule 144. There are two “private” resale exemptions that the affiliate may use – Rule 144A and the Section 4(a)(1½) exemption.

- Why are these “private” resales?
 - Because the transferee will receive a restricted security, or a security subject to contractual restrictions on transfer.
- Rule 144A:
 - Transfers to qualified institutional buyers (“QIBs”);
 - Transferee’s security is a restricted security under Rule 144(a)(3)(iii);
 - All conditions of Rule 144A must be met; some securities and issuers may not be eligible;
 - General solicitation is now allowed, provided that sales are made only to QIBs.

Rule 144A Private Resales

- Why isn't a Rule 144A resale a distribution, causing the seller to be a statutory underwriter? Isn't the transferor acquiring securities from the issuer "with a view to distribution"?
 - 144A resales are not offered to the public;
 - Consequently, they are not distributions, even though the purchaser of the security from the issuer purchased the securities with a view to reselling them;
 - 144A resellers are therefore not underwriters;
 - Persons other than issuers or dealers can rely on Section 4(a)(1), and dealers can rely on Section 4(a)(3) for their 144A resales; and
 - The issuer's Section 4(a)(2) exemption is not tainted by a public distribution.

The “4(a)(1½) exemption”

- The Section 4(a)(1½) exemption has evolved in practice, without the benefit of any official rulemaking.
- It is a hybrid consisting of:
 - A Section 4(a)(1) exemption which exempts transactions by anyone other than an “issuer, underwriter or dealer,” and
 - A Section 4(a)(2) analysis to determine whether the seller is an “underwriter,” *i.e.*, whether the seller purchased the securities with a view to a distribution.
- In 1980, the SEC recognized the section 4(a)(1½) exemption, which although not specifically provided for in the Securities Act “[is] clearly within its intended purpose,” provided that the established criteria for sales under both sections 4(a)(1) and 4(a)(2) are satisfied.

When is the “4(a)(1½) exemption” used?

- The Section 4(a)(1½) exemption can be used by institutional investors to resell restricted securities purchased in a private placement.
- The Section 4(a)(1½) exemption can also be used by affiliates for the sale of control securities when Rule 144 is unavailable.
- It is still used for resales to accredited investors.

How are 4(a)(1½) sales structured?

- In a Section 4(a)(1½) transaction:
 - The seller must sell in a “private” offering to an investor that satisfies the qualifications (for example, sophistication, access to information, etc.) of an investor in a Section 4(a)(2) private offering, and
 - The investor must agree to be subject to the same restrictions imposed on the seller in relation to the securities (for example, securities with a restricted legend).
- Given that a Section 4(a)(1½) transaction seeks to replicate a statutory private placement, it is our view that general solicitation cannot be used in connection with this transaction.

Common practices for 4(a)(1½) sales

- Because the 4(a)(1½) exemption seeks to recreate the conditions that enabled the original private placement, a number of common practices have emerged among practitioners in connection with 4(a)(1½) transactions, including:
 - Purchaser agrees to resale restrictions and make representations and warranties regarding its sophistication and investment intent;
 - Inquiring into the identity of the purchaser, including its financial condition, in order to assess the likelihood that the purchaser will be able to hold the securities for investment and not resell prematurely;
 - Legal opinions confirming the view that no registration is required;
 - Restrictive legends on the securities to alert the purchaser to the restricted nature of the securities;
 - Stop transfer instructions from the issuer;
 - Reselling the restricted securities in large minimum denominations or investments to bolster the purchaser's claims regarding its sophistication and investment intent.

New exemption for resales

- The FAST Act codifies a specific resale exemption, Section 4(a)(7)
- With so many issuers choosing to defer their IPOs and finance their growth through private placements, we now have many more very large, well-financed privately held companies
 - Employees, consultants, angel investors and friends and family investors in these companies require liquidity opportunities
 - More private secondary market transactions are getting done; however, lack of certainty with respect to the Section 4(a)(1½) exemption, as well as blue sky concerns, led to calls to codify a resale exemption
 - The provisions that were incorporated into the FAST Act originally were introduced in the House as the RAISE Act
- This does not replace Section 4(a)(1½) however for certain transfers not involving institutions, it does provide certainty

New exemption for resales (cont'd)

- The exemption will provide certainty for transactions that meet the following requirements:
 - Each purchaser is an accredited investor;
 - Neither the seller nor any person acting on the seller's behalf engages in any form of general solicitation; and
 - In the case of an issuer that is not a reporting company, exempt from the reporting requirements pursuant to Rule 12g3-2(b), or a foreign government eligible to register securities on Schedule B, at the request of the seller, the seller and a prospective purchaser obtain from the issuer reasonably current information, including:
 - The issuer's exact name (as well as the name of any predecessor);
 - The address of the issuer's principal place of business;
 - The exact title and class of the offered security, its par or stated value, and the current capitalization of the issuer;
 - Details for the transfer agent or other person responsible for stock transfers;
 - A statement of the nature of the issuer's business that will be presumed current if it is as of 12 months before the transaction date;

New exemption for resales (cont'd)

- The issuer's officers and directors;
- Information about any broker, dealer or other person being paid a commission or fee in connection with the sale of the securities;
- The issuer's most recent balance sheet and profit and loss statement and similar financial statement for the two preceding fiscal years during which the issuer has been in business, prepared in accordance with GAAP or, in the case of a foreign issuer, IFRS. The balance sheet will be deemed reasonably current if it is as of a date not less than 16 months before the transaction date and the profit and loss statement shall be deemed reasonably current if it is as of a date not less than 12 months preceding the date of the issuer's balance sheet. If the balance sheet is not as of a date less than six months before the transaction date, it must be accompanied by additional statements of profit and loss for the period from the dates of such balance sheet to a date less than six months before the transaction date; and
- If the seller is an affiliate, a statement regarding the nature of the affiliation accompanied by a certification from the seller that it has no reasonable grounds to believe that the issuer is in violation of the securities laws or regulations.

New exemption for resales (cont'd)

- The new Section 4(a)(7) exemption is not available:
 - If the seller is a direct or indirect subsidiary of the issuer;
 - If the seller or any person that will be compensated in connection with the transaction, such as a broker-dealer, is subject to the bad actor disqualification provisions included in Rule 506 or described under Section 3(a)(39) of the Exchange Act;
 - If the issuer is blank check, blind pool, shell company, special purpose acquisition company, or in bankruptcy or receivership;
 - The transaction relates to an broker-dealer's or underwriter's unsold allotment; or
 - The security that is the subject of the transaction is part of a class of securities that has not been authorized and outstanding for at least 90 days prior to the transaction date.
- The securities sold in a Section 4(a)(7) resale transaction will be considered "restricted securities" and "covered securities" for blue sky purposes.
- A transaction effected pursuant to this exemption will not be deemed to be a "distribution" under the Securities Act.

Why choose to rely on Section 4(a)(7)?

- Section 4(a)(7) provides much more flexibility than
 - Rule 144A – resales may only be made to QIBs and Rule 144A is only available in respect of certain securities
 - Rule 144 – resales may only be made in compliance with the holding period, volume and manner of sale requirements
 - Section 4(a)(1½) – as discussed, a private reseller can sell securities in excess of the Rule 144 volume limits
- However, it is important to keep in mind that
 - 4(a)(7) requires that the class of securities have been outstanding for 90 days
 - Securities sold in reliance on Section 4(a)(7) will be “restricted securities” as opposed to having securities sold under Rule 144 which become fungible with publicly traded stock
 - Section 4(a)(7) has an information requirement, which may not be appealing to privately held companies. Section 4(a)(1½) does not
 - Will holders use Rule 144 and Section 4(a)(7) to dispose of their securities

Execution

- Transactions are likely to be effected as block trades with a placement agent acting on an agency basis
- There likely will be a sales agency agreement or engagement letter between the seller and the placement agent
- A securities purchase agreement will be required between private seller and new purchaser
- Placement agent may sell over the course of a few days or have identified demand

Client Alert

December 7, 2015



FAST Forward

A Summary of the Securities Law Provisions of the FAST Act

On December 4, 2015, President Obama signed the Fixing America's Surface Transportation Act ("FAST Act"), which includes a number of securities law related provisions that had previously been the subject of individual bills that had received bipartisan support. Below we summarize these provisions.

Amendments to, or Enhancements to, the JOBS Act

Public Filing Prior to Road Show

Section 71001 of the FAST Act amends Section 6(e)(1) of the Securities Act of 1933 (the "Securities Act"), reducing the 21-day period to a 15-day period during which an emerging growth company, or EGC, must have publicly filed its IPO registration statement prior to commencing its road show. Many market participants supported this change, noting that given ready access to information, 15 days is a sufficient period during which the public can review and access an IPO issuer's registration statement.

EGC Grace Period

Section 71002 further amends Section 6(e)(1) of the Securities Act to provide a grace period permitting an issuer that qualified as an EGC at the time it made its first confidential submission of its IPO registration statement and subsequently during the IPO process ceases to be an EGC to continue to be treated as an EGC through the earlier of:

- the date on which the issuer consummates its IPO pursuant to that registration statement, or
- the end of the one-year period beginning on the date the company ceases to be an EGC.

Omission of Financial Statements

Section 71003 amends Section 102 of the Jumpstart Our Business Startups Act ("JOBS Act") by requiring that within 30 days of enactment of the FAST Act the Securities and Exchange Commission (the "Commission") revise the instructions to Form S-1 and Form F-1 in order to permit, and effective 30 days after enactment of the FAST Act permits, an issuer that is filing a registration statement or submitting a registration statement for confidential review to omit financial information for historical periods that otherwise would be required by Regulation S-X at the time of filing or submission, provided that the omitted financial information will not be required to be included in the Form S-1 or F-1 at the time of the consummation of the offering, and that prior to distribution of a preliminary prospectus to investors, the registration statement includes all required financial statements.

This change may have the most significant impact on IPO costs. Often an issuer is required to devote resources to preparing financial statements and related disclosures for periods solely to comply with the form requirements, although such financial statements and related disclosures will be replaced in an amendment to the registration statement by more current financial statements.

Exchange Act Threshold

Section 85001 of the FAST Act remedies an inadvertent omission in the JOBS Act, which had amended the Securities Exchange Act of 1934 (the “Exchange Act”) Section 12(g) trigger for banks and bank holding companies, by modifying the Section 12(g) Exchange Act trigger for savings and loan holding companies. Now, savings and loan holding companies and banks will be treated the same, and will not be required to register under the Exchange Act unless they have, at the end of the fiscal year, at least \$10 million in assets and a class of equity securities held of record by at least 2,000 persons.

Form 10-K and Regulation S-K

Section 72001 of the FAST Act requires that within 180 days following enactment of the Act, the Commission issue regulations permitting issuers to submit a summary page on Form 10-K if each item identified in the summary includes a cross-reference to the relevant information.

Section 72002 requires that within 180 days following enactment of the Act, the Commission take action to revise Regulation S-K to scale or eliminate requirements to reduce the burden for EGCs, accelerated filers, smaller reporting companies and other smaller issuer and to eliminate provisions of Regulation S-K that are repetitive, outdated or otherwise unnecessary.

Section 72003 requires that the Commission undertake a study of Regulation S-K and in doing so consult with the Investor Advisory Committee and the Advisory Committee on Small and Emerging Companies. Within 360 days following enactment, the Commission shall issue a report to Congress regarding its findings and detailed its recommendations for simplification of the Regulation S-K requirements and the Commission shall issue proposed rules to implement its recommendations. The Commission undertook a similar report as it was mandated to do pursuant to the JOBS Act. In recent public statements various Commissioners and members of the Staff of the Commission have noted that the Staff is already engaged in a disclosure simplification review process. It is not clear how or whether these provisions of the FAST Act would change the process that is already ongoing on disclosure simplification.

Revisions to Form S-1

Section 84001 of the FAST Act requires that within 45 days of enactment, the Commission revise Form S-1 to permit smaller reporting companies to incorporate by reference in a Registration Statement on Form S-1 Exchange Act filings, or “forward incorporate,” made after the effectiveness of the Form S-1. For smaller issuers that are required to use Form S-1 as a “resale shelf” this will be an important change. Currently, such issuers must file post-effective amendments for the purpose of keeping a resale shelf on Form S-1 current, which can be costly.

A New Resale Exemption

Section 76001 of the FAST Act incorporates the provisions of the RAISE Act, which codifies an exemption for certain resales of securities as new Section 4(a)(7). This resale exemption is similar in certain respects to the current “Section 4(a)(1-1/2) exemption” for private resales of restricted securities; however, it is limited in its scope.

The exemption will provide certainty for transactions that meet the following requirements:

- Each purchaser is an accredited investor;
- Neither the seller nor any person acting on the seller’s behalf engages in any form of general solicitation; and
- In the case of an issuer that is not a reporting company, exempt from the reporting requirements pursuant to Rule 12g3-2(b), or a foreign government eligible to register securities on Schedule B, at the request of the seller, the seller and a prospective purchaser obtain from the issuer reasonably current information, including:
 - The issuer’s exact name (as well as the name of any predecessor);
 - The address of the issuer’s principal place of business;
 - The exact title and class of the offered security, its par or stated value, and the current capitalization of the issuer;
 - Details for the transfer agent or other person responsible for stock transfers;
 - A statement of the nature of the issuer’s business that will be presumed current if it is as of 12 months before the transaction date;
 - The issuer’s officers and directors;

- Information about any broker, dealer or other person being paid a commission or fee in connection with the sale of the securities;
- The issuer's most recent balance sheet and profit and loss statement and similar financial statement for the two preceding fiscal years during which the issuer has been in business, prepared in accordance with GAAP or, in the case of a foreign issuer, IFRS. The balance sheet will be deemed reasonably current if it is as of a date not less than 16 months before the transaction date and the profit and loss statement shall be deemed reasonably current if it is as of a date not less than 12 months preceding the date of the issuer's balance sheet. If the balance sheet is not as of a date less than six months before the transaction date, it must be accompanied by additional statements of profit and loss for the period from the dates of such balance sheet to a date less than six months before the transaction date; and
- If the seller is an affiliate, a statement regarding the nature of the affiliation accompanied by a certification from the seller that it has no reasonable grounds to believe that the issuer is in violation of the securities laws or regulations.

The new Section 4(a)(7) exemption is not available:

- If the seller is a direct or indirect subsidiary of the issuer;
- If the seller or any person that will be compensated in connection with the transaction, such as a broker-dealer, is subject to the bad actor disqualification provisions included in Rule 506 or described under Section 3(a)(39) of the Exchange Act;
- If the issuer is blank check, blind pool, shell company, special purpose acquisition company, or in bankruptcy or receivership;
- The transaction relates to an broker-dealer's or underwriter's unsold allotment; or
- The security that is the subject of the transaction is part of a class of securities that has not been authorized and outstanding for at least 90 days prior to the transaction date.

The securities sold in a Section 4(a)(7) resale transaction will be considered "restricted securities" and "covered securities" for blue sky purposes. A transaction effected pursuant to this exemption will not be deemed to be a "distribution" under the Securities Act.

In our view, most resale transactions that are undertaken in reliance on the Section 4(a)(1-1/2) exemption are unlikely to be affected by the availability of this new Section 4(a)(7) exemption given that these generally are transactions entered into between large institutional investors and involve the securities of SEC-reporting companies, as to which current information is readily available.



For a jump start on the JOBS Act, please visit our MoFoJumpstarter blog: www.mofojumpstarter.com. For more updates, follow Thinkingcapmarkets, our Twitter feed: www.twitter.com/Thinkingcapmks.

Authors

David M. Lynn
Washington, D.C.
(202) 887-1563
dlynn@mofo.com

Anna T. Pinedo
New York
(212) 468-8179
apinedo@mofo.com

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Because of the generality of this update, the information provided herein may not be applicable in all situations and should not be acted upon without specific legal advice based on particular situations.

Client Alert

January 15, 2016

SEC Adopts Interim Final Rules to Implement FAST Act Provisions

By David M. Lynn

On January 13, 2016, the Securities and Exchange Commission (the “SEC”) adopted interim final rules to implement Sections 71003 and 84001 of the Fixing America’s Surface Transportation Act (the “FAST Act”). The interim final rules implement revisions to Form S-1 and Form F-1 that permit an emerging growth company to omit financial information from a registration statement for certain periods, provided that all of the required information is included in the registration statement prior to distributing a preliminary prospectus, and revisions to Form S-1 and Item 512 of Regulation S-K that permit a smaller reporting company to incorporate by reference into a Form S-1 any reports or materials filed with the SEC subsequent to the effective date of the registration statement.

The interim final rules are effective upon publication in the *Federal Register*. The SEC deadline for comments on the interim final rules is 30 days following publication in the *Federal Register*.

HISTORICAL FINANCIAL STATEMENT REQUIREMENTS FOR EGCS

Section 71003 amended Section 102 of the Jumpstart Our Business Startups Act (the “JOBS Act”) to permit an emerging growth company¹ that is filing a registration statement or submitting a registration statement for confidential review to omit financial information for historical periods that otherwise would be required by Regulation S-X at the time of filing or submission, provided that the issuer reasonably believes that the omitted financial information will not be required to be included in the Form S-1 or F-1 at the time of the consummation of the offering, and that prior to distribution of a preliminary prospectus to investors, the registration statement includes all required financial statements. The SEC was directed to revise the instructions to Form S-1 and Form F-1 in order to permit this change within 30 days of enactment of the FAST Act.

¹ An “emerging growth company” is defined in Section 2(a)(19) of the Securities Act to mean an issuer with less than \$1 billion in total annual gross revenues during its most recently completed fiscal year. If an issuer qualifies as an emerging growth company on the first day of its fiscal year, it maintains that status until the earliest of the last day of the fiscal year of the issuer during which it has total annual gross revenues of \$1 billion or more; the last day of its fiscal year following the fifth anniversary of the first sale of its common equity securities pursuant to an effective registration statement; the date on which the issuer has, during the previous 3-year period, issued more than \$1 billion in non-convertible debt; or the date on which the issuer is deemed to be a “large accelerated filer” (as defined in Exchange Act Rule 12b-2). Section 71002 of the FAST Act (which was effective upon enactment of the FAST Act) amends Section 6(e)(1) of the Securities Act to provide that an issuer that qualifies as an emerging growth company at the time it initiates the registration process, either by submitting a draft registration statement or by filing it publicly, but which subsequently ceases to be an emerging growth company, will continue to be treated as an emerging growth company until the earlier of the date on which the issuer consummates its initial public offering pursuant to that registration statement or the end of the 1-year period beginning on the date the company ceases to be an emerging growth company.

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The SEC has revised Form S-1 by adding General Instruction II.C., which states:

A registration statement filed (or submitted for confidential review) under Section 6 of the Securities Act (15 U.S.C. 77f) by an emerging growth company, defined in Section 2(a)(19) of the Securities Act (15 U.S.C. 77b(a)(19)), prior to an initial public offering may omit financial information for historical periods otherwise required by Regulation S-X (17 CFR Part 210) as of the time of filing (or confidential submission) of the registration statement, provided that:

1. The omitted financial information relates to a historical period that the registrant reasonably believes will not be required to be included in this Form at the time of the contemplated offering; and
2. Prior to the registrant distributing a preliminary prospectus to investors, the registration statement is amended to include all financial information required by Regulation S-X at the date of the amendment.

Similar language was adopted as General Instruction II.E. to Form F-1, which differs from the Form S-1 instruction in that it references both Regulation S-X and Item 8.A. of Form 20-F when describing the applicable financial statement requirements.

This provision of the FAST Act and the amendments adopted by the SEC will allow emerging growth companies to reduce the costs incurred in public offerings by permitting the exclusion of historical financial statements that will eventually be superseded by more recent financial statements by the time the marketing of the offering commences through the distribution of a preliminary prospectus.

In Question 2 of the SEC Staff's *Fixing America's Surface Transportation (FAST) Act Compliance and Disclosure Interpretations*, the Staff noted that an EGC may omit financial statements of other entities from its filing or submission if it reasonably believes that those financial statements will not be required at the time of the offering, therefore the relief would apply, for example, to the financial statements of an acquired business required by Rule 3-05 of Regulation S-X if the emerging growth company reasonably believes those financial statements will not be required at the time of the offering. In Question 1 of the *Fixing America's Surface Transportation (FAST) Act Compliance and Disclosure Interpretations*, that Staff noted that an emerging growth company may not omit interim financial statements from its filing or submission for a period that has financial information that will be included within required financial statements covering a longer interim or annual period at the time of the offering, even though the shorter period will not be presented separately at that time. In the Division of Corporation Finance announcement *Recently Enacted Transportation Law Includes a Number of Changes to the Federal Securities Laws*, the Division stated that the Staff would not object if EGCs apply Section 71003 immediately after enactment of the FAST Act.

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FORWARD INCORPORATION BY REFERENCE FOR EGCS

Section 84001 of the FAST Act requires that, within 45 days of enactment, the Commission revise Form S-1 to permit a smaller reporting company² to incorporate by reference in a Registration Statement on Form S-1 filings made under the Securities Exchange Act of 1934, as amended (the “Exchange Act”), or “forward incorporate,” made after the effectiveness of the Form S-1.

The SEC amended Item 12 of Form S-1 to include new paragraph (b), which states:

In addition to the incorporation by reference permitted pursuant to paragraph (a) of this Item, a smaller reporting company, as defined in Rule 405 (17 CFR 230.405), may elect to incorporate by reference information filed after the effective date of the registration statement. A smaller reporting company making this election must state in the prospectus contained in the registration statement that all documents subsequently filed by the registrant pursuant to Sections 13(a), 13(c), 14 or 15(d) of the Exchange Act, prior to the termination of the offering shall be deemed to be incorporated by reference into the prospectus.

As a result, under the interim final rules, a smaller reporting company must meet each of the existing eligibility requirements and conditions for incorporation by reference in order to utilize the new forward incorporation by reference provisions in Form S-1. In this regard, a smaller reporting company must have filed:

- an annual report for its most recently completed fiscal year; and
- all required Exchange Act reports and materials during the 12 months immediately preceding filing of the Form S-1 (or such shorter period during which the smaller reporting company was required to file such reports and materials).

In addition, a smaller reporting company relying on the new forward incorporation by reference provision must make its incorporated Exchange Act reports and other materials readily available and accessible on a web site maintained by or for the issuer and disclose in the prospectus that such materials will be provided upon request.

Smaller reporting companies that are blank check companies, shell companies (other than business combination related shell companies) or issuers for offerings of penny stocks will not be permitted to forward incorporate by reference information into a Form S-1.

The SEC also made a conforming change to Item 512(a) of Regulation S-K to provide for forward incorporation by reference of Exchange Act reports filed or furnished after the effective date of the registration statement on Form S-1. The undertakings in Item 512(b) of Regulation S-K will also be required in Form S-1 registration statements filed by smaller reporting companies that use forward incorporation by reference.

² A “smaller reporting company” is defined in Rule 405 under the Securities Act to mean an issuer that had a public float of less than \$75 million as of the last business day of its most recently completed second fiscal quarter or had annual revenues of less than \$50 million during the most recently completed fiscal year for which audited financial statements are available.



Regulation A+: Final Rules Offer Important Capital Raising Alternatives

Overview

Yesterday, March 25, 2015, the Securities and Exchange Commission voted unanimously to adopt final rules to implement the rulemaking mandate of Title IV of the JOBS Act by adopting amendments to Regulation A. In December 2013, the SEC had released a proposed rule that essentially retained the current framework of Regulation A and expanded it for larger exempt offerings. The proposed rules were generally well-received. The final rules addresses a number of issues raised by commenters, while retaining substantially the same approach outlined in the proposed rule.

Briefly, by way of background, existing Regulation A provides an exemption from the registration requirements of Section 5 for certain smaller securities offerings by private (non-SEC-reporting) companies. The securities sold in a Regulation A offering are not considered “restricted securities” and are freely transferable. However, the low dollar threshold, the disclosure requirements, and the requirement to comply with state blue sky laws had limited the utility of Regulation A. Other exemptions, such as Rule 506 under Regulation D, which have no dollar threshold, became more popular. Prior to the JOBS Act, a number of market participants advocated amending Regulation A to raise the dollar threshold and legislation to amend and to modernize Regulation A was proposed and considered prior to the emergence of the JOBS Act. In large measure, Title IV of the JOBS Act incorporated many of the provisions that had been addressed in those standalone bills. Section 401 of the JOBS Act amended Section 3(b) of the Securities Act by renumbering it as Section 3(b)(1) and adopting new sections (b)(2) through (b)(5). Pursuant to the JOBS Act additions to Section 3(b), the SEC is authorized to promulgate rules or regulations creating an exemption that is substantially similar to the existing Regulation A for offerings of up to \$50 million.

The New Regulation A

As discussed in more detail below, the final rules provide an exemption for U.S. and Canadian companies that are not required to file reports under the Exchange Act to raise up to \$50 million in a 12-month period. The final rules create two tiers: Tier 1 for smaller offerings raising up to \$20 million in any 12-month period, and Tier 2 for offerings raising up to \$50 million. The new rules also make the exemption available, subject to limitations on the amount, for the sale of securities by existing stockholders. The new rules modernize the existing framework under Regulation A by, among other things, requiring that disclosure documents be filed on EDGAR, allowing an issuer to make a confidential submission with the SEC, permitting certain test-the-waters communications, and disqualifying bad actors. The final rules impose different disclosure requirements for Tier 1 and Tier 2 offerings,

with more disclosure required for Tier 2 offerings, including audited financial statements. Tier 1 offerings will be subject to both SEC and state blue sky pre-sale review. Tier 2 offerings will be subject to SEC, but not state blue sky, pre-sale review; however, investors in a Tier 2 offering will be subject to investment limits (except when securities are sold to accredited investors or are listed on a national securities exchange) and Tier 2 issuers will be required to comply with periodic filing requirements, which include a requirement to file current reports upon the occurrence of certain events, semi-annual reports and annual reports. The final rules provide a means for an issuer in a Tier 2 offering to concurrently list a class of securities on a national exchange through a short-form Form 8-A, without requiring the filing of a separate registration statement on Form 10.

Eligible Issuers

The new Regulation A exemption, both Tier 1 and Tier 2, will be available to issuers organized in and having their principal place of business in the United States or Canada. The following issuers will be “ineligible” to offer or sell securities under Regulation A:

- (1) an issuer that is an SEC-reporting company;
- (2) a blank check company;
- (3) any investment company registered or required to be registered under the Investment Company Act of 1940 (this includes business development companies); and
- (4) any entity issuing fractional undivided interests in oil or gas rights, or similar interests in other mineral rights.

The exemption also is not available to: issuers that have not filed with the SEC the ongoing reports required by Regulation A during the two years immediately preceding the filing of a new offering statement, issuers that have had their registration revoked pursuant to an Exchange Act Section 12(j) order that was entered into within five years before the filing of the offering statement and certain bad actors.

Eligible Securities

The securities that may be offered under Regulation A are limited to equity securities, including warrants, debt securities and debt securities convertible into or exchangeable into equity interests, including any guarantees of such securities. The final rule excludes asset-backed securities.

Offering Limitations

As noted above, an issuer can choose a Tier 1 or a Tier 2 offering. Under Tier 1, an issuer may offer and sell up to \$20 million in a 12-month period, of which up to \$6 million may constitute secondary sales (except as noted below). Under Tier 2, an issuer may offer and sell up to \$50 million in a 12-month period, of which up to \$15 million may constitute secondary sales (except as noted below). The final rules set out an approach for calculating the offering limit in the case of convertible or exchangeable securities.

In the issuer’s initial Regulation A offering and any Regulation A-exempt offering in the 12 months following that offering price of the particular offering, the selling securityholder component cannot exceed 30% of the aggregate offering. In addition, the final rules distinguish between sales by affiliates and sales by non-affiliates. Following the expiration of the first year following an issuer’s initial qualification of a Regulation A offering statement, the limit on secondary sales falls away for non-affiliates only. Notably, the final rule eliminates the current prohibition on resales by affiliates in reliance on the exemption unless the issuer had net income from continuing operations in at least one of the last two years.

Investment Limitation

Prior to the amendments, Regulation A did not contain a limit on the amount of securities that may be purchased by an investor. However, to address potential investor protection concerns, the final rules impose an investment limit for Tier 2 offerings. The investment limit will not apply to accredited investors and will not apply if the securities are to be listed on a national securities exchange at the consummation of the offering; otherwise a non-accredited natural person is subject to an investment limit and must limit purchases to no more than 10% of the greater of the investor's annual income and net worth, determined as provided in Rule 501 of Regulation D (for non-accredited, non-natural persons, the 10% limit is based on annual revenues and net assets).

Investors must be notified of the investment limitations, and may rely on a representation of compliance with the investment limitation from the investor, unless the issuer knew at the time of sale that any such representation is untrue.

Integration of Offerings

A Regulation A offering will not be integrated with:

- (1) prior offers or sales of securities; or
- (2) subsequent offers or sales of securities that are:
 - (i) registered under the Securities Act, except as provided in Rule 255(e);
 - (ii) made in reliance on Rule 701;
 - (iii) made pursuant to an employee benefit plan;
 - (iv) made in reliance on Regulation S;
 - (v) made pursuant to Section 4(a)(6) of the Securities Act [crowdfunded offerings]; or
 - (vi) made more than six months after the completion of the Regulation A offering.

As a result, one could envision an issuer making a private offering under Section 4(a)(2) or Regulation D prior to commencing a Regulation A offering without risking integration of the private offering with the Regulation A offering. An offering made under Regulation A should not be integrated with another exempt offering, provided that each exempt offering complies with the requirements for the exemption that is being relied upon for that particular offering. The final rule also addresses abandoned offerings in much the same way that these are handled by Rule 155, with a 30-day cooling off period.

The SEC reaffirmed guidance that was included in the proposing release which is consistent with the guidance regarding integration provided in Release 33-8828.

Exchange Act Threshold

The proposed rule did not exempt securities sold pursuant to Regulation A from the calculation of "holder of record" for purposes of the Section 12(g) Exchange Act threshold. The final rule, however, provides a limited exemption for securities issued in a Tier 2 offering from the Section 12(g) "holder of record" threshold where the issuer is subject to, and current in its, Regulation A periodic reporting obligations. In order to benefit from this conditional exemption, an issuer must: retain the services of a transfer agent and meet requirements similar to

those in the “smaller reporting company” definition (public float of less than \$75 million or, in the absence of a float, revenues of less than \$50 million, in the most recently completed fiscal year). An issuer that exceeds the Section 12(g) threshold will have a two-year transition period.

Filing and Delivery Requirements

Regulation A offering statements must be filed on EDGAR. The Form 1-A has been amended to consist of three parts: Part I, which will be an XML-based fillable form with basic issuer information; Part II, which will be a text file that will contain the disclosure document and financial statements; and Part III, which will be a text file that will contain exhibits and related materials. Periodic reports and any other documents required to be submitted to the SEC in connection with a Regulation A offering must be filed on EDGAR.

As proposed, the final rules adopts an access equals delivery model for Regulation A final offering circulars. In the case where a preliminary offering circular is used to offer securities to potential investors and the issuer is not already subject to the Tier 2 periodic reporting requirements, an issuer and participating broker-dealer will be required to deliver the preliminary offering circular to prospective purchasers at least 48 hours in advance of sales.

Non-Public Review

An issuer may submit an offering statement for non-public review by the SEC. As with EGCs, should an issuer opt for confidential review, the offering statement must be filed publicly not less than 21 calendar days before qualification of the offering statement. The timing, in the case of a Regulation A offering, is not tied to an issuer’s road show, but rather to the qualification of the offering statement. The SEC noted specifically that the 21-day public filing period will provide state securities regulators an opportunity to assure filing of offering materials at the state level in advance of an offering under Regulation A.

Form 1-A

An issuer that seeks to rely on Regulation A must file and qualify an offering statement. The offering statement is intended to be a disclosure document that provides potential investors with information that will form the basis for their investment decision. A notice of “qualification” is similar to a notice of effectiveness in an SEC-registered offering.

Part I

As noted above, Part I requires certain basic information regarding the issuer, its eligibility, the offering details, the jurisdictions where the securities will be offered, and sales of unregistered securities.

Part II

Part II contains the narrative portion of the Offering Circular and requires disclosures of basic information about the issuer; material risks; use of proceeds; an overview of the issuer’s business; an MD&A type discussion; disclosures about executive officers and directors and compensation; beneficial ownership information; related party transactions; and a description of the offered securities. This is similar to Part I of Form S-1, and an issuer can choose to comply with Part I of Form S-1 in connection with its Offering Circular. The disclosure requirements will be scaled.

Tier 1 and Tier 2 issuers must file balance sheets and other required financial statements as of the two most recently completed fiscal year ends (or for such shorter time as they have been in existence). U.S. issuers are required to prepare financial statements in accordance with U.S. GAAP. Canadian issuers may

use U.S. GAAP or IFRS as adopted by the IASB. As with EGCs, an issuer may elect to delay implementation of new accounting standards to the extent such standard permit delayed implementation by non-public business entities. The election is a one-time election and must be disclosed.

The financial statements for an issuer in a Tier 1 offering are not required to be disclosed; however, if a Tier 1 issuer already obtained an audit of its financial statement for other purposes and such audit was performed in accordance with U.S. GAAS or the PCAOB standards and the auditors meet the independence standards, then the audited financial statements must be filed.

The financial statements for an issuer in a Tier 2 offering are required to be audited. The audit firm must satisfy the independence standard but need not be PCAOB-registered. The financial statements may be audited in accordance with either U.S. GAAS or PCAOB standards. An issuer in a Tier 2 offering that seeks to have a class of securities listed on a national securities exchange concurrent with the Regulation A offering must include financial statements prepared in accordance with PCAOB standards by a PCAOB-registered firm.

The final rule addresses technical matters, such as the age of the financial statements. Issuers in Tier II offerings are not required to provide financial statements in an interactive data format using XBRL.

Part III

The exhibit requirements in Part III of Form 1-A are maintained, however, the final rule allows for incorporation by reference of exhibits that were previously filed on EDGAR.

Continuous Offerings

The final rule would continue to permit continuous or delayed offerings in certain instances, such as for offerings offered or sold on behalf of selling security holders, securities offered under employee benefit plans; securities pledged as collateral; securities issued upon conversion of other outstanding securities or upon the exercise of options, warrants, or rights, etc.; or securities that are part of an offering which commences within two calendar days after the qualification date, will be offered on an continuous basis, may continue to be offered for a period in excess of 30 days from the date of initial qualification, and will be offered in an amount that, at the time the offering statement is qualified, is reasonably expected to be offered and sold within a period of two years from the initial qualification date. The offerings permitted under Regulation A would be limited in the same manner as under Rule 415; as such, delayed offerings would not be permitted under Regulation A.

Offering Communications

An issuer engaged in a Regulation A offering has substantial flexibility regarding offering communications. An issuer must file solicitation materials with the SEC. Solicitation materials used after an offering circular is filed must be accompanied by the offering circular or include a link to the offering circular. Solicitation materials will be subject to certain legends.

The SEC also confirmed that regularly released factual business communications will not constitute solicitation materials, consistent with the guidance of Rule 169.

Ongoing Reporting Requirements

Currently, Regulation A does not require that issuers file ongoing reports with the SEC, other than a Form 2-A to report sales or termination of sales made under Regulation A. While the final rules rescind Form 2-A, they impose new on-going reporting obligations for certain offerings.

Tier 1 issuers will be required to provide certain information about their Regulation A offerings on a new form, Form 1-Z.

Issuers in Tier 2 offerings will be subject to an ongoing reporting regime. Similar to the ongoing reporting regime that the SEC proposed in connection with issuers that conduct crowdfunded offerings, Tier 2 issuers would be required to file:

- annual reports on Form 1-K;
- semi-annual reports on Form 1-SA;
- current reports on Form 1-U;
- special financial reports on Form 1-K and Form 1-SA; and
- exit reports on Form 1-Z.

The Form 1-K would require disclosures relating to the issuer's business and operations for the preceding three fiscal years (or since inception if in existence for less than three years); related party transactions; beneficial ownership; executive officers and directors; executive compensation; MD&A; and two years of audited financial statements. The form is required to be filed within 120 calendar days of the issuer's fiscal year-end.

The semi-annual report would be similar to a Form 10-Q, although it would be subject to scaled disclosure requirements. The semi-annual report is required to be filed within 90 days after the end of the first six months of the issuer's fiscal year end, commencing immediately following the most recent fiscal year for which full financial statements were included in the offering circular or, if the offering circular included six-month interim financial statements for the most recent full fiscal year, then for the first six months of the following fiscal year.

A current report on Form 1-U will be required to announce fundamental changes in the issuer's business; entry into bankruptcy or receivership proceedings; material modifications to the rights of securityholders; changes in accountants; non-reliance on audited financial statements; changes in control; changes in key executive officers; and sales of 10 percent or more of outstanding equity securities in exempt offerings. The form must be filed within four business days of the triggering event.

An exit report on Form 1-Z would be required to be filed within 30 days after the termination or completion of a Regulation A-exempt offering.

Rule 15c2-11, Rule 144 and Rule 144A

A Tier 2 issuer's periodic reports will satisfy Exchange Act Rule 15c2-11 broker-dealer requirements relating to the obligation to review information about an issuer in connection with publishing quotations on any facility other than a national securities exchange. However, contrary to commenters' requests, the final rule does not establish that these reports would constitute "current information" for Rule 144 and Rule 144A purposes. A Tier 2 issuer that voluntarily submits quarterly information in a form consistent with that required for semi-annual information would be able to satisfy the "reasonably current information" and "adequate current public information" requirements.

Tier 2 Offering with Concurrent Exchange Act Registration

The final rules facilitate the ability of a Tier 2 issuer to voluntarily register a class of Regulation A securities under the Exchange Act. In the absence of the relief provided in the final rules, an issuer that completed a Regulation A offering and sought to list a class of securities on a national securities exchange would have had to incur the costs and the timing delays associated with preparing and filing a separate registration statement on Form 10. The final

rule permits a Tier 2 issuer that has provided disclosure in Part II of Form 1-A that follows Part 1 of Form S-1 (or for REITs, Form S-11) to file a Form 8-A to list its securities on a national securities exchange. Of course, thereafter, the issuer would be subject to Exchange Act reporting requirements. An issuer that enters the Exchange Act reporting regime in this manner will be an EGC.

Termination or Suspension of Tier 2 Disclosure Obligations

Tier 2 issuers would be permitted to terminate or suspend their ongoing reporting obligations on a basis similar to the provisions for suspension or termination of reporting requirements for Exchange Act filers. A Tier 2 issuer that has filed all required ongoing reports for the shorter of: (1) the period since the issuer became subject to such reporting obligations, or (2) its most recent three fiscal years and the portion of the current year preceding the date of filing Form 1-Z (termination or exit form) will be permitted to suspend its reporting obligations at any time after completing reporting for the fiscal year in which the offering statement was qualified. This suspension will be permitted if the securities of each class to which the offering statement relates are held of record by fewer than 300 persons and offers or sales made in reliance on a qualified offering statement are not ongoing. Further, the Regulation A on-going reporting requirements would be automatically suspended if an issuer registers a class of securities under Section 12 of the Exchange Act.

Bad Actor Disqualification Provisions

The final rule includes bad actor disqualification provisions that are largely consistent with those included in Rule 506(d).

State Securities Law Requirements

As discussed above, one of the most significant concerns regarding the use of the Regulation A exemption has been the requirement to comply with state securities laws. At the time the new rules were proposed, there was no coordinated review process by the states for Regulation A offerings. Although NASAA has now introduced a coordinated review process for Regulation A offerings since the new rules were proposed, the SEC noted that the coordinated review process is relatively new and it remains largely untested.

The final rules provide that Tier 1 offerings will remain subject to state securities law requirements. Consistent with the proposed rules, Tier 2 offerings will not be subject to state review if the securities are sold to “qualified purchasers” or, as provided by statute in the JOBS Act, listed on a national securities exchange. The final rule defines the term “qualified purchaser” in a Regulation A offering to include: all offerees and purchasers in a Tier 2 offering. States will, of course, continue to have authority to require filing of offering materials and enforce anti-fraud provisions in connection with a Tier 2 offering.

Securities Act Liability

Sellers of Regulation A securities would have Section 12(a)(2) liability in respect of offers or sales made by means of an offering circular or oral communications that include a material misleading statement or omission. While an exempt offering pursuant to Regulation A is excluded from the operation of Section 11 of the Securities Act, those offerings are subject to the antifraud provisions under the federal securities laws.

Character of the Securities Sold in a Regulation A Offering

The securities sold in a Regulation A offering are not considered “restricted securities” under Securities Act Rule 144. As a result, sales of the securities by persons who are not affiliates of the issuer would not be subject to any transfer restrictions under Rule 144. Affiliates, of course, would continue to be subject to the limitations of Rule 144, other than the holding period requirement. This is important to an issuer that would like an active trading

market to develop for its securities following completion of a Regulation A offering. However, the issuer's securities may not be listed or quoted on a securities exchange without registration under Section 12 of the Exchange Act, and, as a result, there may not be a liquid market for the securities.

Effective Date

The final rules will be effective 60 days following publication in the Federal Register.

FINRA Review

For any public offering of securities, FINRA Rule 5110 prohibits FINRA members and their associated persons from participating in any manner unless they comply with the filing requirements of the rule.¹ Rule 5110 also contains rules regarding underwriting compensation. Rule 5110(b) requires that certain documents and information be filed with and reviewed by FINRA, and these filing and review requirements apply to securities offered under Regulation A.²

Additional Information

We will be supplementing this alert with additional materials, as well as offering various client briefings.

¹ See FINRA Rule 5110.

² See NASD Notice to Members 92-28 (May 1992); see also NASD Notice to Members 86-27 (Apr. 1986).

Summary Charts

Below we provide two charts. The first chart summarizes the provisions of current Regulation A, the final rules governing Tier 1 Offerings under the final rule and the final rules governing Tier 2 Offerings. The second chart provides a summary comparison of various securities exemptions.

	Prior Regulation A Exempt Public Offering	Tier 1 of New Regulation A+	Tier 2 of New Regulation A+
Offering Limit	Up to \$5 million within the prior 12-month period.	Up to \$20 million in a 12-month period.	Up to \$50 million in a 12-month period.
SEC Filing Requirements	Must file with the SEC a Form 1-A, which is reviewed and qualified by the SEC.	Must file with the SEC a Form 1-A, which must be reviewed and qualified by the SEC.	Must file with the SEC a Form 1-A, which must be reviewed and qualified by the SEC.
Blue Sky Requirements	Blue sky law compliance is required, without, in many cases, the possibility for a more streamlined “registration by coordination” process.	Blue sky law compliance is required, with the newly implemented NASAA coordinate review process available.	Exempt from state law review, subject to state filing and anti-fraud authority, for offerings to qualified purchasers or where securities are listed on an national securities exchange.
Limitations on Investors	No limits on investors, except to the extent imposed under state laws.	No limits.	Investment limit applicable for persons who are not accredited investors.
Restrictions on Resale of Securities	No restrictions on the resale of securities, except to the extent that the securities are held by affiliates.	No restrictions on the resale of securities, except to the extent that the securities are held by affiliates.	No restrictions on the resale of securities, except to the extent that the securities are held by affiliates.
Offering Communications	An issuer may “test the waters” to determine if there is interest in a proposed offering prior to filing the Form 1-A. Sales literature may be used before the filing of the Form 1-A, after filing, and following qualification.	An issuer may “test the waters” to determine if there is interest in a proposed offering prior to filing the Form 1-A. Sales literature may be used before the filing of the Form 1-A, after filing, and following qualification.	An issuer may “test the waters” to determine if there is interest in a proposed offering prior to filing the Form 1-A. Sales literature may be used before the filing of the Form 1-A, after filing, and following qualification.
Financial Statement Requirements	A current balance sheet, as well as income statements for a period of two years, as well as any interim period. Financial statements must be prepared in accordance with GAAP but do not have to conform to Regulation S-X and, in most cases, do not have to be audited.	<ul style="list-style-type: none"> Audited financial statements only if prepared for other purposes. If audited, then must be audited by an independent accountant, but not required to be PCAOB-registered. Current balance sheet, income statement for two years, as well as any interim period. 	<ul style="list-style-type: none"> Audited financial statements required, reviewed by an independent accountant and prepared in accordance with PCAOB standards. Current balance sheet, income statement for two years, as well as any interim period.
Disqualification Provisions	Felons and bad actors disqualified from the offering in accordance with Securities Act Rule 262.	Felons and bad actors disqualified; Rule 262 updated.	Felons and bad actors disqualified; Rule 262 updated.
Ongoing Reporting	No reporting required after the offering, other than to disclose the use of proceeds.	A termination report required.	Subject to on-going reporting obligation, including a requirement to file: current reports, semi-annual reports; and annual reports, until obligations are terminated or suspended.

Type of Offering	Dollar Limit	Manner of Offering	Issuer and Investor Requirements	Filing Requirement	Restriction on Resale	Blue Sky Exemption
Section 3(a)(11)	None.	No limitation other than to maintain intrastate character of offering.	All issuers and investors must be resident in state. No limitation on number.	None.	Rests within the state (generally a one-year period for resales within state).	Need to comply with state blue sky laws by registration or state exemption.
Section 4(a)(2)	None.	No general solicitation or general advertising.	All issuers and investors must meet sophistication and access to information test so as not to need protection of registration.	None.	Restricted securities.	Need to comply with state blue sky laws.
Rule 504 Regulation D	\$1 million within prior 12 months.	No general solicitation or general advertising unless registered in a state requiring use of a substantive disclosure document or sold under state exemption for sales to accredited investors with general solicitation.	No requirements.	File Form D with the Commission not later than 15 days after first sale. Filing not a condition of the exemption.	Restricted unless registered in a state requiring use of a substantive disclosure document or sold under state exemption for sale to accredited investors with general solicitation.	Need to comply with state blue sky laws by registration or state exemption.
Rule 505 Regulation D	\$5 million within prior 12 months	No general solicitation or advertising.	Unlimited accredited investors and 35 non-accredited investors.	File Form D with the Commission not later than 15 days after first sale. Filing not a condition of the exemption.	Restricted securities.	Need to comply with state blue sky laws.
Rule 506 Regulation D	None.	No general solicitation or advertising under Rule 506(b). General solicitation and general advertising permitted under Rule 506(c), provided all purchasers are accredited investors.	Under Rule 506(b), unlimited accredited investors and 35 non-accredited investors. Under Rule 506(c), all purchasers must be accredited investors.	File Form D with SEC not later than 15 days after first sale. Filing not a condition of the exemption.	Restricted securities.	No need to comply with state blue sky laws.
Tier 1 Regulation A	\$20 million within prior 12 months, but no more than \$6 million by selling security holders.	“Testing the waters” permitted before and after filing Form 1-A. Sales permitted after Form 1-A qualified.	Eligible Issuer No investor requirement.	File test-the-waters documents, Form 1-A, any sales material and report of sales and use of proceeds with the SEC.	Not restricted securities.	Subject to state blue sky laws regarding pre-offering review, filing, and anti-fraud.

<p>Tier 2 Regulation A</p>	<p>\$50 million within the prior 12 months, but no more than \$15 million by selling security holders.</p>	<p>“Testing the waters” permitted before and after filing Form 1-A. Sales permitted after Form 1-A qualified.</p>	<p>Eligible Issuer No investor requirement; however, investors who are natural persons and are not non-accredited investors are subject to an investment limit.</p>	<p>File test-the-waters documents, Form 1-A, any sales material and report of sales and use of proceeds with the SEC. Issuer subject to ongoing reporting requirements.</p>	<p>Not restricted securities.</p>	<p>Not subject to state blue sky laws regarding pre-offering review; however, subject to state blue sky filing and anti-fraud requirements.</p>
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MOFO JUMPSTARTER

For a jump start on the JOBS Act, please visit our MoFoJumpstarter blog: www.mofojumpstarter.com.

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Authors

Marty Dunn
Washington, D.C.
(202) 778-1611
mdunn@mofo.com

David M. Lynn
Washington, D.C.
(202) 887-1563
dlynn@mofo.com

Anna T. Pinedo
New York
(212) 468-8179
apinedo@mofo.com

James R. Tanenbaum
New York
(212) 468-8163
jtannenbaum@mofo.com

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Client Alert

POTENTIAL FUTURE RULEMAKING

The SEC noted in the adopting release for the interim final rules that while the amendments apply to emerging growth companies omitting financial information from Form S-1 or Form F-1 and to smaller reporting companies using forward incorporation by reference in Form S-1, the Staff will consider whether the amendments discussed in this release should be made available to a larger group of registrants, and for additional form types. The SEC notes that any future rulemaking proposal that stems from the Staff's consideration would be subject to notice and public comment.

The adopting release also solicits comments on any aspect of our interim final rules, other matters that might have an impact on the rules, and any suggestions for additional changes.

Contact:

David M. Lynn
(202) 887-1563
dlynn@mofo.com

Anna T. Pinedo
(212) 468-8179
apinedo@mofo.com

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Following the Wisdom of the Crowd?

A Look at the SEC's Final Crowdfunding Rules

In this alert, we provide a detailed overview of the final rules, Regulation Crowdfunding, which will be applicable to crowdfunding offerings conducted in reliance on Section 4(a)(6) of the Securities Act of 1933 as amended (the "Securities Act"), which was added by Title III of the Jumpstart Our Business Startups Act of 2012 (the "JOBS Act"), as well as to those intermediaries participating in such offerings. We do not address the proposed FINRA framework applicable to funding portals, which will be covered in a separate alert. All rule references, unless otherwise noted, refer to rules under Regulation Crowdfunding.

We will supplement this alert with a more detailed practical analysis comparing the various new offering exemptions available to issuers as a result of the JOBS Act.

PART ONE: GENERAL REQUIREMENTS

Limit on Capital Raised

Consistent with the statutory limitations, Rule 100(a) provides that an issuer may sell up to \$1 million in any 12-month period to investors in an offering made pursuant to the exemption. Of course, an issuer may consider conducting other exempt offerings in close proximity with its crowdfunded offering. In calculating the amounts sold for purposes of the threshold, amounts sold by a predecessor or by an entity under common control with the issuer will be aggregated with the amounts sold by the issuer.

Individual Investment Limits

In the final rules, the Securities and Exchange Commission (the "SEC") has modified the investor limits from those included in its proposed rules. The final rules make clear that the individual investor limit is an aggregate limit, which applies to all investments made by the individual over a 12-month period in crowdfunded offerings and not to a specific offering.

An investor will be limited to investing:

- (1) The greater of: \$2,000 or 5% of the lesser of the investor's annual income or net worth if either annual income or net worth is less than \$100,000; or
- (2) 10% of the lesser of the investor's annual income or net worth, not to exceed an amount sold of \$100,000, if both annual income and net worth are \$100,000 or more.

As we discuss below, the issuer can rely on the intermediary's calculation of the investment limit; provided that the issuer does not have knowledge that the investor has exceeded, or would exceed, the investment limits as a result of participating in the issuer's offering.

Offering through an Intermediary

An issuer would only be able to engage in an offering through a registered broker-dealer or through a funding portal, and an issuer can only use one intermediary for a particular offering or concurrent offerings made in reliance on the exemption.

The offering must be conducted online only through the intermediary's platform, so that the "crowd" has access to information and there is a forum for an exchange of information among potential offering participants.

A "platform" is defined as "a program or application accessible via the Internet or other similar electronic communication medium through which a registered broker or a registered funding portal acts as an intermediary in a transaction involving the offer or sale of securities in reliance on Section 4(a)(6) of the Securities Act."

Eligible Issuers

The ability to engage in crowdfunding is not available to all issuers. By statute, the following issuers cannot rely on crowdfunding transactions under Section 4(a)(6):

- issuers not organized under the laws of a state or territory of the United States or the District of Columbia;
- issuers already subject to Securities Exchange Act of 1934, as amended (the "Exchange Act") reporting requirements;
- investment companies as defined in the Investment Company Act of 1940 (the "Investment Company Act") or companies that are excluded from the definition of "investment company" under Section 3(b) or 3(c) of the Investment Company Act; and
- any issuer that the Commission, by rule or regulation, determines appropriate.

The final rules also exclude:

- issuers disqualified from relying on Section 4(a)(6), or "bad actors;" and
- issuers that have sold securities in reliance on Section 4(a)(6) and have failed, to the extent required, to make required ongoing reports required by Regulation Crowdfunding during the two-year period immediately preceding the filing of the required new offering statement; and

- any issuer that is a development stage company that has no specific business plan or purpose, or has indicated that its business plan is to engage in a merger or acquisition with an unidentified company or companies.

PART TWO: ISSUER REQUIREMENTS

Disclosure Requirements

The statute sets out a number of required disclosures in any Section 4(a)(6) offering. An issuer that elects to engage in a crowdfunding offering must comply with disclosure requirements, including: an initial disclosure about the offering on Form C, amendments to Form C to report material changes (Form C-A), periodic updates on the offering on Form C-U and ongoing annual filings until a filing obligation is terminated. The annual filing must be made on Form C-AR and a termination notice on Form C-TR.

Form C

The Form C would be filed with SEC and the intermediary would post the filing or provide a link to the filing for investors. The Form C must include disclosures relating to the issuer's business, officers, directors and control persons, use of proceeds, capital structure and financial results, as discussed below in more detail. In many respects, the Form C requirements resemble those for Form 1-A used in connection with Regulation A offerings. The final Form C also includes an optional Q&A format that issuers may elect to use to provide certain disclosures.

Basic issuer information would be required, including: the entity name, the form of entity, the jurisdiction of formation, formation date, address, website, number of employees, the issuer's website on which an investor can find the issuer's annual report and the date by which such report will be made available, whether the issuer or any predecessor previously failed to comply with the ongoing reporting requirements of Regulation Crowdfunding. In addition, the form must disclose certain basic information about the intermediary, including: the intermediary's SEC file number and FINRA CRD number and fees being paid to the intermediary, expressed either as a dollar amount or as a percentage of the offering amount, and a description of the intermediary's financial interests in the transaction and in the issuer.

In addition, the form will require, among other things, a discussion of:

- **Use of Proceeds:** a specific use or range of possible uses for the offering proceeds, as well as the factors impacting the selection by the issuer of each such use;
- **The Targeted Offering Size:** as discussed further below, the issuer must disclose the maximum offering size and the subscription process;
- **Offering Price:** a description of the price to the public of the securities and a description of how the offered securities were valued;
- **Business:** the form must include a business description, for which no particular format is prescribed;
- **Directors and officers:** each individual's name, positions held with the issuer and duration in those positions and business experience during the last three years;

- **Beneficial Ownership and Capital Structure:** for principal stockholders, the issuer would be required to identify each shareholder who owns 20% or more of the issuer's outstanding voting equity securities (calculated as of the most recent practicable date), as well as provide a description of capital stock, including any special voting rights or investor rights;
- **Indebtedness;**
- **Related party transactions:** a description of transactions that involve amounts in excess of 5% of the amount raised by the issuer in crowdfunded offerings in the trailing 12-month period including in the proposed deal;
- **Exempt offerings:** a description of all exempt offerings undertaken during the preceding three years;
- **Risk factors:** a discussion of risks associated with an investment in the securities and with participation in a crowdfunded offering;
- **Transfer restrictions;** and
- **Management's Discussion and Analysis:** a discussion that covers each period for which financial statements of the issuer are provided, as well as a discussion of material changes or trends known to management.

Financial Statement Requirements

In a change from the proposed rules, the final rules provide some accommodations with respect to financial statement requirements depending upon the target offering size and for first-time issuers.

Based on target offering size, the requirements are as follows:

- **\$100,000 or less:** the amount of total income, taxable income and total tax or equivalent line items, as reported on the federal tax forms filed by the issuer for the most recently completed year (if any), certified by the principal executive officer of the issuer, and the financial statements of the issuer, also certified by the principal executive officer. If financial statements of the issuer are available that have either been reviewed or audited by a public accountant independent of the issuer, then, these financial statements must be provided instead of the materials described in the preceding sentence.
- **More than \$100,000 and less than \$500,000:** financial statements of the issuer reviewed by a public accountant independent of the issuer. If financial statements of the issuer are available that have been audited by a public accountant independent of the issuer, the issuer must provide those instead of the reviewed statements.
- **More than \$500,000:** financial statements of the issuer audited by a public accountant independent of the issuer; provided, however, that for issuers that are first-time issuers, offerings that have a target offering amount of more than \$500,000 but not more than \$1 million, financial statements of the issuer reviewed by a public accountant independent of the issuer. If audited statements are available, those must be provided instead.

Financial statements must be prepared in accordance with U.S. GAAP. Audited financial statements must be conducted in accordance either with American Institute of Certified Public Accountants ("AICPA") standards (referred to as U.S. GAAS) or Public Company Accounting Oversight Board

(“PCAOB”) standards. These requirements are similar to those applicable for Tier 1 offerings made under Regulation A. A signed audit report must accompany audited financial statements.

During the first 120 days of the issuer’s fiscal year, an issuer may conduct an offering in reliance on Section 4(a)(6) using financial statements for the fiscal year prior to the most recently completed fiscal year if the financial statements for the most recently completed fiscal year are not otherwise available.

Amendments to Form C

An issuer would be required to amend its Form C disclosures using Form C/A for any updates or material changes. The materiality determination is left up to the issuer based on the customary guidance that the SEC considers a material change to be a change that would affect an investor’s investment decision. The issuer must identify on Form C/A whether the amendment is filed to disclose a material change. Investor reconfirmations must be obtained following the occurrence of a material change.

Progress Update

An issuer also is required to file progress updates with the SEC on a Form C-U. Updates are required five days after any of the following milestones: commitments for 50% of the deal are received, commitments for the full deal are received, subscriptions in excess of the initial offering amount will be accepted, or the issuer closes the offering.

Annual Report

An issuer that completes a crowdfunded offering must file with the SEC and post on its website an annual report on Form C-AR along with financial statements of the issuer certified by its principal executive officer within 120 days of the end of the issuer’s fiscal year. The annual report is required to contain the same information required in the offering statement, described above.

Termination of Reporting

An issuer must file with the SEC a Form C-TR to terminate its reporting obligation within five days of the date on which it becomes eligible to do so.

An issuer can terminate its ongoing reporting requirements upon the earliest to occur of the following:

- the issuer is required to file reports under the Exchange Act;
- the issuer has filed at least one annual report and has fewer than 300 holders of record;
- the issuer has filed at least three annual reports and has total assets that do not exceed \$10 million;
- the issuer or another party purchases or repurchases all of the securities issued pursuant to Section 4(a)(6), including any payment in full of debt securities or any complete redemption of redeemable securities; or
- the issuer liquidates or dissolves in accordance with state law.

Offering Amount and Offering Mechanics

In connection with a proposed offering, the rules contemplate that the issuer would include in its disclosures a discussion of the target or maximum amount to be raised, and a discussion of the subscription or offering process. The description of the subscription process must disclose that investors can cancel their investment up to 48 hours prior to the deadline identified in the offering materials, but if an investor does not cancel the investment, then the investor's funds will be released to the issuer upon closing.

The intermediary will notify investors when the target offering amount has been met, and if the target offering amount is not met, then no securities will be sold and all funds will be returned to investors. If the target offering amount is met prior to the deadline identified in the offering materials, the issuer must provide five days' advance notice before closing the offering early. If an investor does not reconfirm the investment commitment after a material change is made to the offering and disclosed on Form C-A, the investment will be cancelled, and the issuer must return the funds to the investor.

Types of Securities Offered

The final rules do not limit the types of securities that may be offered in reliance on Section 4(a)(6). The release notes that an issuer may offer debt securities and discusses the exemption from the requirement to qualify an indenture under the Trust Indenture Act of 1939 (the "Trust Indenture Act") for any offering exempted by Section 4 of the Securities Act from the provisions of Section 5 of the Securities Act; however, the final rules do not include a specific exemption from Trust Indenture Act requirements for crowdfunded offerings.

Status of Securities

Securities sold in a crowdfunded offering pursuant to the exemption would be subject to transfer restrictions. Pursuant to Rule 501, securities issued in a crowdfunded offering could not be transferred by a purchaser for one year from the date of purchase, except for transfers to: the issuer; an accredited investor; a family member of the purchaser or in estate type transfers; and third parties in an SEC-registered offering.

The statute exempts securities sold in Section 4(a)(6) offerings from the Exchange Act "holder of record" count for the purposes of determining if registration of a class of equity securities is required under Section 12(g). An issuer will be required to establish a means for tracking its shareholders. This may require an early-stage company to engage the services of a transfer agent or other similar service provider in order to monitor its security holders.

Integration

An offering made pursuant to the Section 4(a)(6) exemption will not be integrated with another exempt offering that precedes the crowdfunded offering or that takes place concurrently or subsequently. The issuer must ensure that it has satisfied all of the conditions for the exemption that it is claiming for each such offering. If the issuer is conducting a Rule 506(c) offering (using general solicitation), it must ensure that the Rule 506(c) offerees were not solicited by means of the communications used for the crowdfunded offering.

Restrictions on Advertising and Promotion

The final rules limit the ability of the issuer, as well as the ability of others acting on the issuer's behalf, to advertise. Pursuant to Rule 204, an issuer is permitted to advertise a Section 4(a)(6)-exempt offering by releasing an offering notice that contains only the following information:

- a statement that the issuer is conducting an offering;
- the name of the intermediary and a link to the intermediary's offering page;
- the amount of securities offered;
- the nature of the securities;
- the price of the securities;
- the closing date for the offering; and
- the name, address, phone number and website of the issuer;
- the email address of a representative of the issuer; and
- a brief factual description of the issuer's business.

The adopting release notes that this notice is intended to be similar to tombstone ads permitted under Securities Act Rule 134. The issuer would be able to communicate with potential crowdfunding investors if the communications occur through the platform; however, it should be clear to potential investors which platform communications are being made by the issuer or on the issuer's behalf.

The final rules do not limit an issuer from being able to continue to engage in regular business communications so long as it does not disclose information about the offering, except as permitted in an offering notice. However, the final rules do not contain an express safe harbor for regularly released business information.

Promoter Compensation

Rule 205 prohibits an issuer from compensating, or committing to compensate, directly or indirectly, a person for advertising or promoting a Section 4(a)(6) offering through the intermediary's platform, unless the issuer takes reasonable steps to ensure that the person clearly discloses the receipt (past and prospective) of compensation each time that such person makes a promotional communication. A founder or employee of the issuer that engages in promotional activities on the issuer's behalf through the intermediary's platform would be required to disclose in each posting that s/he is engaging in those activities on the issuer's behalf.

The release discusses a number of "reasonable steps" that an issuer can take in order to ensure that promoters disclose the receipt of communication, including, but not limited to, obtaining representations from the promoter and monitoring communications.

PART THREE: INTERMEDIARIES

Title III of the JOBS Act provides that a crowdfunded offering must be made through an intermediary that is either a registered broker-dealer or a funding portal. The intermediary is intended to function as a gatekeeper and, in this role, protect investors from fraud. The SEC's final rules establish a regulatory framework for these intermediaries. As discussed below, in the case of funding portals, the regulatory framework is a scaled back version of the framework applicable to broker-dealers.

We discuss the final rules in the sequence of an offering and then provide an overview of the registration, compliance and other requirements applicable to intermediaries.

Conducting a Crowdfunded Offering

Single Intermediary

As discussed above, the final rules require that an offering be made only through one intermediary.

Financial Interests in Issuer

Rule 300 prohibits directors, officers or partners (or others having a similar status or performing a similar function) of an intermediary from having any financial interest in an issuer using its services and prohibits such persons from receiving a financial interest in an issuer as compensation for the service provided to or for the benefit of the issuer in connection with the offering. An intermediary cannot have a financial interest in an issuer that is using the intermediary's platform, unless:

- The intermediary receives the financial interest from the issuer as offering compensation; and
- The financial interest consists of securities of the same class and having the same terms as those sold in the offering.

A "financial interest" in an issuer means a direct or indirect ownership of, or economic interest in, any class of the issuer's securities.

Measures to Reduce Risk of Fraud

Under Rule 301, an intermediary must have a reasonable basis for believing that the issuer is in compliance with relevant regulations and has established means to keep accurate records of holders of the securities it offers. An intermediary could reasonably rely on the issuer's representations, absent knowledge or other information that would suggest that the representations are not true.

An intermediary must deny access to an issuer if it has a reasonable belief that the issuer or its offering would present a potential for fraud. An intermediary would be required to deny access to its platform to an issuer if the intermediary has a reasonable belief that the issuer, or any of its directors, officers or 20% beneficial owners is subject to a disqualification under Rule 503. An intermediary must conduct a background and securities enforcement regulatory history check on each issuer whose securities are to be offered by the intermediary, as well as on each of its officers, directors (or any person occupying a similar status or performing a similar function) and 20% beneficial owners.

Account Opening

Under Rule 302, no intermediary or associated person may accept an investment commitment until the investor opens an account with the intermediary and the intermediary obtains consent to electronic delivery of materials. An intermediary is required to certain information to each investor, including educational materials, by electronic message with links to information posted on the intermediary's website.

Educational Materials

Rule 302 requires that in connection with establishing an account, an intermediary deliver educational materials in plain English. Any revised materials must be made available to all investors before accepting any additional investment commitments or effecting any further crowdfunded transactions. The materials must discuss:

- the process for the offering;
- the types of securities sold through the platform and the associated risks;
- the restrictions on resale;
- the offering statement;
- the investment limitations;
- the limitations on an investor's right to cancel an investment commitment and the circumstances under which an issuer may cancel the commitment;
- the need to consider the appropriateness for the investor of an investment in a crowdfunded offering;
- that following the completion of the offering there may or may not be a continuing relationship between the issuer and the intermediary; and
- that under certain circumstances the issuer may cease its ongoing reporting.

An intermediary also would be required to inform investors that disclosure is required regarding any past or prospective compensation paid to a promoter. An intermediary also must disclose the compensation it will receive in connection with crowdfunded offerings.

Issuer Information

Under Rule 303, an intermediary must make available to the SEC and potential investors not later than 21 days prior to the first day on which securities are sold to any investor any information provided by the issuer under Rules 201 and 203(a).

The information must be made publicly available on the intermediary's platform, in a manner that reasonably permits a person accessing the platform to save, download or store the information; this information be made publicly available on the intermediary's platform for a minimum of 21 days before any securities are sold in the offering, during which time the intermediary may accept investment commitments; and this information, including any additional information provided by the issuer, remain publicly available on the intermediary's platform until the offer and sale is completed or cancelled. An intermediary cannot require any person to establish an account with the intermediary in order to receive this information.

Investor Qualifications

Securities Act Section 4A(a)(8) imposes an obligation on intermediaries to make sure no investor exceeds the statutory investment limitations.

The final rules implement this requirement by providing that, before permitting an investor to make an investment commitment on its platform, an intermediary must have a reasonable basis to believe that the investor satisfies the investment limitations discussed above.

The final rules allow reasonable reliance on an investor's representation to this effect.

Investor's Acknowledgment of Risks

Securities Act Section 4A(a)(4) requires an intermediary to ensure that each investor reviews the educational materials, positively affirms that the investor understands that he or she is risking the loss of the entire investment and that the investor could bear such a loss, and answer questions demonstrating an understanding of the level of risk involved in startups. As discussed above, educational materials must be provided at account opening.

Rule 303 requires that an intermediary, each time before accepting an investment commitment, obtain from the investor a representation that the investor has reviewed the intermediary's educational materials, understands that the entire investment may be lost and can bear the risk of loss. The intermediary also must ensure each time before accepting an investment commitment that each investor answers questions demonstrating the investor's understanding that there are restrictions on the investor's ability to cancel an investment commitment and obtain a return of his or her investment, that it may be difficult for the investor to resell the securities and that the investor should not invest any funds in a crowdfunding offering unless s/he can afford to lose the entire amount of his or her investment.

Communication Channels

Rule 303 requires an intermediary to provide, on its platform, channels through which investors can communicate with one another and with representatives of the issuer about offerings made available on the intermediary's platform, subject to certain conditions.

This is intended to provide a centralized and transparent means for members of the public to share their views and to communicate with the issuer. The intermediary cannot participate in the communications. It can set rules regarding the postings or remove postings that use offensive language.

Communications should be available for public viewing, but the intermediary would only be able to permit those persons who have opened accounts with it to post comments. With each post, a person must disclose whether such person is a promoter or affiliate of the issuer and whether it has been or will be compensated. The intermediary must keep records of these communications.

Notice of Investment Commitment

An intermediary, upon receipt of an investment commitment from an investor, must promptly give or send to the investor a notification disclosing: the dollar amount of the commitment, the price of the securities (if known), the name of the issuer and the date and time by which the investor may cancel the investment commitment. Notification would be required to be provided by email or other electronic media and to be documented in accordance with applicable recordkeeping rules.

Maintenance and Transmission of Funds

Securities Act Section 4A(a)(7) requires that an intermediary “ensure that all offering proceeds are only provided to the issuer when the aggregate capital raised from all investors is equal to or greater than a target offering amount.”

An intermediary that is a registered broker must comply with established requirements in Exchange Act Rule 15c2-4 for the maintenance and transmission of investor funds. Investor funds must be held in escrow until the specified contingency occurs (*i.e.*, the targeted amount or the minimum amount is raised), and then the funds would be promptly transmitted to a bank, which has agreed in writing to hold such funds in escrow for the investors and to transmit or return such funds directly to the issuer or to investors, as the case may be. Proceeds are to be transmitted to the issuer only if the target offering amount is met or exceeded.

Because a funding portal cannot receive or handle any funds, it would be required to direct investors to transmit money or other consideration directly to a qualified third party (a registered broker-dealer, a bank, or a credit union) that serves as an escrow agent. A funding portal must promptly direct transmission of funds from the qualified third party to the issuer when the aggregate amount of investment commitments from all investors is equal to or greater than the target amount of the offering and the cancellation period for each investor has expired, but no earlier than 21 days after the date on which the intermediary makes publicly available on its platform the information required to be provided about the issuer and the offering. A funding portal must direct the return of funds to an investor when an investment commitment has been cancelled or the offering is terminated or cancelled.

Confirmation of Transaction

At or before the completion of a transaction, the intermediary is required to give or send each investor a notification, like a confirmation, disclosing the transaction date; the type of security; the price and number of securities purchased; the number of securities sold by the issuer in the transaction; the price at which the securities were sold; certain specified terms of the security (for example, if it is a debt or callable security); and the source and amount of any remuneration received or to be received by the intermediary in connection with the transaction, whether from the issuer or other persons. This notification must be by email or other electronic media and subject to recordkeeping rules.

Completion of Offerings, Cancellations and Reconfirmations

Investors have an unconditional right to cancel an investment commitment for any reason until 48 hours prior to the deadline identified in the issuer’s offering materials. Thereafter, an investor cannot cancel any investment commitments made within the final 48 hours (except in the event of a material change to the offering, as discussed below).

If an issuer reaches the target offering amount prior to the deadline identified in its offering materials, it may close the offering once the target offering amount is reached, provided that the offering will have remained open for a minimum of 21 days; the intermediary provides notice about the new offering deadline at least five business days prior to the new offering deadline; investors are given the opportunity to reconsider their investment decision and to cancel their investment commitment until

48 hours prior to the new offering deadline; and at the time of the new offering deadline, the issuer continues to meet or exceed the target offering amount.

If there is a material change to the terms of the offering, or the information provided by the issuer regarding the offering, the intermediary must give or send to any potential investors who have made investment commitments notice of the material change, stating that the investor's investment commitment will be cancelled unless the investor reconfirms his or her commitment within five business days of receipt of the notice. If the investor fails to reconfirm his or her investment within those five business days, the intermediary, within five business days thereafter, must provide or send the investor a notification disclosing that the investment commitment was cancelled, the reason for the cancellation and the refund amount that the investor should expect to receive, and direct the refund of investor funds.

Finally, if an issuer does not complete an offering because the target is not reached or the issuer decides to terminate the offering the intermediary within five business days must give or send to each investor who made an investment commitment a notification disclosing the cancellation of the offering, the reason for the cancellation, the refund amount that the investor should expect to receive, direct the refund of investor funds and prevent investors from making investment commitments with respect to that offering on its platform.

Intermediary Registration and Other Requirements

Registration and SRO Membership

An intermediary must be registered as a broker-dealer with the SEC under Section 15(b) of the Exchange Act or a funding portal registered with the SEC in accordance with the requirements of Rule 400 and also a member of a national securities association registered under Section 15A of the Exchange Act, which is FINRA.

Additional Requirements on Funding Portals

The SEC has established a streamlined registration process under which a funding portal would register with the SEC by filing a form, Form Funding Portal, with information consistent with, but less extensive than, the information required for broker-dealers on Form BD.

A funding portal would register by completing a Form Funding Portal, which includes information concerning the funding portal's principal place of business, its legal organization and its disciplinary history, if any; business activities, including the types of compensation the funding portal has received and disclosure of its disciplinary history, if any; FINRA membership with any other registered national securities association; and the funding portal's website address(es) or other means of access.

A funding portal's registration would become effective the later of (1) 30 calendar days after the date that the registration is received by the SEC; or (2) the date the funding portal is approved for membership in FINRA.

In order to promote transparency, all such Forms Funding Portal will be available publicly.

A funding portal must file an amendment to the Form Funding Portal within 30 days of any of the information in the original form becoming inaccurate for any reason. The final rules require a funding portal to promptly file a withdrawal of registration on Form Funding Portal upon ceasing to operate as a funding portal. The withdrawal would be effective on the later of 30 days after receipt by the SEC after the funding portal is no longer operational within such longer period of time as to which the funding portal consents or within such period of time as to which the SEC, by order, may determine as necessary or appropriate in the public interest or for the protection of investors.

A funding portal can operate multiple website addresses under a single funding portal registration provided that the funding portal discloses on the Form Funding Portal all the website and names under which it does business.

Non-U.S. Funding Portals

Entities domiciled or organized outside of the United States (“nonresident funding portals”) are able to act as funding portals; however, they are subject to additional requirements.

There must be an information sharing arrangement in place between the SEC and the competent regulator in the jurisdiction under the laws of which the nonresident funding portal is organized or where it has its principal place of business. In addition, a nonresident funding portal would be required to have an agent for service of process in the United States, as well as an opinion of counsel addressing the ability of the applicant to provide the SEC and the national securities association of which it is a member with prompt access to its books and records and to submit to onsite inspection and examination by the SEC and the national securities association. The nonresident funding portal also would be required to consent that service of any civil action brought by, or notice of any proceeding before, the SEC or any national securities association of which it is a member, in connection with the funding portal’s investment-related business, may be given by registered or certified mail to the nonresident funding portal’s contact person at the main address or mailing address indicated on the form.

Fidelity Bond

The proposed rules would have required a fidelity bond, however the final rules do not require a fidelity bond.

Exemptions from Broker-Dealer Registration and Safe Harbors

But for the exemption from registration for funding portals that Congress directed in the JOBS Act, a funding portal would be required to register as a broker under the Exchange Act.

The SEC’s final rules exempt an intermediary that is registered as a funding portal from the requirement to register as a broker-dealer under the Exchange Act, although a funding portal would remain subject to the full range of the SEC’s examination and enforcement authority.

A funding portal cannot:

- Offer investment advice or recommendations;

- Solicit purchases, sales or offers to buy the securities displayed on its platform;
- Compensate employees, agents or other persons for such solicitations based on the sale of securities displayed or referenced on its platform; or
- Hold, manage, possess or otherwise handle investor funds or securities.

In addition, the final rules set out certain “permitted activities” of a funding portal.

Providing Communication Channels: as noted above, a funding portal should provide a channel for potential investors to communicate about the merits of an offering.

Highlighting Issuers and Offerings: a funding portal may highlight a particular offering made through its platform based on objective criteria, such as the type of security, geographic region, industry, etc. Criteria must be objective and cannot be based on investment advice or implicitly endorse an issuer or an offering. The funding portal cannot receive special or additional compensation for highlighting one or more issuers or offerings on its platform.

Advising Issuers: a funding portal may advise an issuer on the structure or content of its proposed offering and prepare offering documentation.

Paying for Referrals: a funding portal may pay for referrals, subject to various limitations.

Compensation Arrangements with Registered Broker-Dealers: a funding portal may enter into arrangements with a broker-dealer pursuant to which they could compensate one another provided such arrangements are not prohibited by the national securities association of which the funding portal is a member.

Advertising: a funding portal could advertise its services as well as offerings that are available through its platform, subject to compliance with various requirements.

Limiting Offerings: a funding portal can limit the offerings on its platforms (for example, by limiting the offerings to issuers in certain industries, geographies, etc.) without being deemed to be providing investment advice. The criteria would be required to be reasonably designed to result in a broad selection of issuers offering securities through the funding portal’s platform and be applied consistently to all potential issuers and offerings. Criteria must be displayed on the funding portal’s site.

Compliance Policies and Procedures

A funding portal is required to implement written policies and procedures designed to achieve compliance with applicable regulations.

A funding portal will be required to comply with the same privacy rules (Regulation S-P, Regulation S-AM, and Regulation S-ID) applicable to broker-dealers.

A funding portal is subject to the SEC's examination and inspection authority. Also, a funding portal is subject to recordkeeping requirements in order to ensure that there is an audit trail for all crowdfunding transactions and communications.

Disqualification ("Bad Actor") Provisions

Rule 503 sets out bad actor disqualification provisions. The Section 4(a)(6) exemption will not be available for a sale of securities if the issuer, a predecessor of the issuer, an affiliated issuer, any director, officer, general partner or managing member of the issuer, a beneficial owner of 20% or more of the issuer's outstanding voting equity securities, any promoter or solicitor, or any general partner, director, officer or managing member of any such solicitor is subject to a "statutory disqualification."

Conclusion

With the much anticipated crowdfunding rules now adopted, it will be interesting to observe the extent to which the rules will prove useful for issuers and intermediaries in raising small amounts of capital. While the SEC sought to add more flexibility in the final rule within the confines of the statutory directive from Title III of the JOBS Act, the exemption contemplates procedural and informational requirements that will require the significant dedication of resources by the smaller issuers that would likely find the exemption most useful, as well as their intermediaries. We will continue to monitor developments as market practices emerge for issuers and intermediaries.

MOFO JUMPSTARTER

For a jump start on the JOBS Act, please visit our MoFoJumpstarter blog: www.mofojumpstarter.com.

Authors

David M. Lynn
Washington, D.C.
(202) 887-1563
dlynn@mofo.com

Anna T. Pinedo
New York
(212) 468-8179
apinedo@mofo.com

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Client Alert

November 5, 2015

SEC Proposes Rule Changes to Pave the Way for Intrastate and Regional Offerings

By David Lynn

At the same time the Securities and Exchange Commission (the “SEC”) adopted rules implementing Regulation Crowdfunding pursuant to Title III of the Jumpstart Our Business Startups Act (the “JOBS Act”), the agency proposed rule changes that could potentially facilitate intrastate and regional offerings that are subject to state blue sky regulation. In particular, the SEC proposed to modernize Rule 147 under the Securities Act of 1933, as amended (the “Securities Act”), and establish a new exemption to facilitate offerings relying upon recently adopted intrastate crowdfunding exemptions under state securities laws. The SEC also proposed amendments to Rule 504 of Regulation D under the Securities Act to increase the aggregate amount of securities that may be offered and sold in any twelve-month period from \$1 million to \$5 million and to disqualify certain bad actors from participating in Rule 504 offerings. The SEC indicated in the proposing release that these proposals are “part of the Commission’s efforts to assist smaller companies with capital formation consistent with other public policy goals, including investor protection.”

PROPOSED AMENDMENTS TO RULE 147

Rule 147 is a safe harbor for intrastate offerings exempt from registration pursuant to Securities Act Section 3(a)(11), which exempts “any security which is a part of an issue offered and sold only to persons resident within a single state or territory, where the issuer of such security is a person residing and doing business within, or, if a corporation, incorporated by and doing business within such state or territory.” The proposed amendments would eliminate the restriction on offers, while continuing to require that sales be made only to residents of an issuer’s state or territory. The proposed amendments also would redefine “intrastate offering” and ease issuer eligibility requirements. The SEC proposes to limit the availability of the exemption to offerings that are either registered in the state in which all of the purchasers are resident, or conducted pursuant to an exemption from state law registration in such state that limits the amount of securities an issuer may sell pursuant to such exemption to no more than \$5 million in a twelve-month period and imposes an investment limitation on investors.

The SEC noted that over time it has been observed that the statutory limitation on offers in Section 3(a)(11) and the prescriptive threshold requirements that an issuer must satisfy in order to be considered “doing business” in-state as specified in Rule 147 have combined to limit the availability of the exemption for companies that otherwise might have considered using the exemption in order to conduct intrastate offerings. In particular, these provisions make it difficult to conduct intrastate offerings utilizing the Internet. The SEC also noted that a number of states have adopted and/or enacted crowdfunding provisions, or currently have crowdfunding legislation pending. These state-based crowdfunding provisions generally require that an issuer, in addition to complying with various state-specific requirements to qualify for the exemption, also comply with Section 3(a)(11) and Rule 147. State securities regulators have indicated to the SEC that Section 3(a)(11) and Rule 147 make it difficult for companies to take advantage of these new crowdfunding provisions.

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The proposed amendments to Rule 147 would permit an issuer to engage in any form of general solicitation or general advertising, including the use of publicly accessible Internet websites, to offer and sell its securities, so long as all sales occur within the same state or territory in which the issuer's principal place of business is located, and the offering is registered in the state in which all of the purchasers are resident, or is conducted pursuant to an exemption from state law registration in such state that limits the amount of securities an issuer may sell pursuant to such exemption to no more than \$5 million in a twelve-month period and imposes an investment limitation on investors. The proposed amendments would also define an issuer's principal place of business (as opposed to its "principal office" as defined in current Rule 147) as the location in which the officers, partners, or managers of the issuer primarily direct, control, and coordinate the activities of the issuer and further require the issuer to satisfy at least one of four threshold requirements discussed below regarding the in-state nature of the issuer's business. As defined, an issuer would only be able to have a "principal place of business" within a single state or territory and would therefore only be able to conduct an offering pursuant to amended Rule 147 within that state or territory. Further, as proposed, the provisions of Rule 147 regarding legends and mandatory disclosures to purchasers and prospective purchasers would be retained.

Rule 147, as it is proposed to be amended, would no longer fall within the statutory parameters of Section 3(a)(11); therefore, the SEC proposed to amend Rule 147 to create an exemption pursuant to the SEC's general exemptive authority under Section 28 of the Securities Act. As proposed to be amended, Rule 147 would function as a separate exemption rather than as a safe harbor under Section 3(a)(11), and Section 3(a)(11) would still be available as a potential statutory exemption in and of itself.

Based on its belief that the rules should continue to require that the securities sold in an intrastate offering in one state should come to rest within such state before sales are permitted to out-of-state residents, the SEC proposes to limit the ability of an issuer that has changed its principal place of business to conduct an intrastate offering in a different state until such time as the securities sold in reliance on the proposed exemption in the prior state have come to rest in that state. For this purpose, the SEC proposes that issuers that have changed their principal place of business after making sales in an intrastate offering pursuant to proposed Rule 147 would not be able to conduct an intrastate offering pursuant to proposed Rule 147 in another state for a period of nine months from the date of the last sale in the prior state, which is consistent with the duration of the resale limitation period specified in proposed Rule 147(e), discussed below.

For the purpose of determining the "in-state" nature of the issuer utilizing Rule 147, the rule as proposed would require that, in addition to the requirement that an issuer have its principal place of business in-state, the issuer must meet at least one of the following requirements (instead of all requirements, as currently specified in Rule 147): (i) the issuer derived at least 80% of its consolidated gross revenues from the operation of a business or of real property located in or from the rendering of services within such state or territory; (ii) the issuer had at the end of its most recent semi-annual fiscal period prior to the first offer of securities pursuant to the exemption, at least 80% of its consolidated assets located within such state or territory; (iii) the issuer intends to use and uses at least 80% of the net proceeds to the issuer from sales made pursuant to the exemption in connection with the operation of a business or of real property, the purchase of real property located in, or the rendering of services within such state or territory; or (iv) a majority of the issuer's employees are based in such state or territory (this fourth prong is proposed to be added to the list).

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While current Rule 147(d) requires that offers and sales of securities pursuant to the rule be made only to persons resident within the state or territory of which the issuer is a resident, so that the exemption would be lost for the entire offering if securities are offered or sold to one investor that was not in fact a resident of the state, the proposed amendments would add a reasonable belief standard to the issuer's determination as to the residence of the purchaser at the time of the sale of the securities. An issuer would satisfy this by either the existence of the fact that the purchaser is a resident of the applicable state or territory, or by establishing that the issuer had a reasonable belief that the purchaser of the securities in the offering was a resident of such state or territory. The SEC also proposes to eliminate the current requirement in Rule 147 that issuers obtain a written representation from each purchaser as to his or her residence.

The proposed amendments also would define the residence of a purchaser that is a legal entity (i.e., a corporation, partnership, trust, or other form of business organization) as the location where, at the time of the sale, the entity has its principal place of business. The proposed amendments would define a purchaser's "principal place of business," consistent with the proposed definition for issuer eligibility purposes, as the location in which the officers, partners, or managers of the entity primarily direct, control and coordinate the activities of the issuer.

Under current Rule 147(e), "during the period in which securities that are part of an issue are being offered and sold by the issuer, and for a period of nine months from the date of the last sale by the issuer of such securities, all resales of any part of the issue, by any person, shall be made only to persons resident within such state or territory." This limitation on resales is designed to help ensure that the securities issued in an intrastate offering have come to rest in the state of the offering before any potential redistribution out-of-state. The SEC proposes to amend the limitation on resales in Rule 147(e) to provide that "for a period of nine months from the date of the sale by the issuer of a security sold pursuant to this rule, any resale of such security by a purchaser shall be made only to persons resident within such state or territory, as determined pursuant to paragraph (d) of this rule." The SEC believes that a nine-month limitation on resales by resident purchasers to non-residents would ensure that the securities purchased by such residents were purchased without a view to further distribution to non-residents. In addition, Rule 147 would be revised so that compliance with Rule 147(e) would not be a condition for the issuer relying on the exemption.

The SEC also proposes to align the integration safe harbor in Rule 147 with the recently adopted integration safe harbor in Rule 251(c) of Regulation A. As proposed, offers and sales made pursuant to Rule 147 would not be integrated with:

- Prior offers or sales of securities; or
- Subsequent offers or sales of securities that are:
 - Registered under the Securities Act, except as provided in Rule 147(h);
 - Exempt from registration under Regulation A;
 - Exempt from registration under Rule 701;
 - Made pursuant to an employee benefit plan;
 - Exempt from registration under Regulation S;

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- Exempt from registration under Section 4(a)(6) of the Securities Act; or
- Made more than six months after the completion of an offering conducted pursuant to Rule 147.

As with Rule 251(c) of Regulation A, the proposed integration safe harbor would expressly provide that any offer or sale made in reliance on the rule would not be integrated with any other offer or sale made either before the commencement of, or more than six months after, the completion of the Rule 147 offering. There would be no presumption that offerings outside the integration safe harbor should be integrated.

The proposing release also indicates that an offering made in reliance on Rule 147 would not be integrated with another exempt offering made concurrently by the issuer, provided that each offering complies with the requirements of the exemption that is being relied upon for the particular offering. Further, consistent with the approach that the SEC took to integration in Rule 251(c), the proposed rules provide that, subject to certain exceptions specified in the rule, offers or sales made in reliance on Rule 147 should not be integrated with subsequent offers or sales that are registered under the Securities Act, or qualified by the SEC pursuant to Regulation A.

PROPOSED REGULATION D AMENDMENTS

Rule 504 of Regulation D currently provides issuers with an exemption from registration for offers and sales of up to \$1 million of securities in a twelve-month period, provided that the issuer is not:

- subject to reporting pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 (the “Exchange Act”);
- an investment company; or
- a blank check company.

Additionally, Rule 504 imposes conditions for the availability of the exemption, including limitations on the use of general solicitation or general advertising in the offering and the restricted status of securities issued pursuant to the exemption, with limited exceptions in this regard for offers and sales made:

- exclusively in one or more states that provide for the registration of the securities, and require the public filing and delivery to investors of a substantive disclosure document before sale that are made in accordance with state law requirements;
- in one or more states that have no provision for the registration of the securities or the public filing or delivery of a disclosure document before the sale, if the securities have been registered in at least one state that provides for such registration, public filing, and delivery before sale, offers and sales are made in that state in accordance with such provisions, and the disclosure document is delivered before sale to all purchasers (including those in the states that have no such procedure); or
- exclusively according to state law exemptions from registration that permit general solicitation and general advertising so long as sales are made only to “accredited investors” as defined in Rule 501(a) of Regulation D.

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Offerings conducted pursuant to Rule 504 must be registered in each state in which they are offered or sold, unless an exemption to state registration is available under state securities laws. Most states require registration of Rule 504 offerings; however, Maine recently adopted a form of state-based crowdfunding that permits the use of general solicitation, but still exempts the issuances of securities from state registration where, in addition to satisfying various state-specific requirements to qualify for the exemption, an issuer also complies with Rule 504 of Regulation D.

The SEC proposes to amend Rule 504 of Regulation D to increase the aggregate amount of securities that may be offered and sold in any twelve-month period from \$1 million to \$5 million and to disqualify certain bad actors from participation in Rule 504 offerings by referencing the disqualification provisions of Rule 506 of Regulation D. The SEC also seeks public comment on whether additional changes to Rule 504 should be adopted. The SEC noted that if the proposed amendments to Rule 504 were adopted, Rule 505 of Regulation D would become less useful, and, therefore, the SEC requests comment on whether Rule 505 should be retained in its current form or in a modified form, or repealed in its entirety.

The SEC believes that the proposed amendments to Rule 504 could provide state securities regulators with greater flexibility to develop regional coordinated review programs that would rely on Rule 504 at the federal level, given that the proposed changes would increase the maximum amount of capital that could be raised while providing states with assurance that certain bad actors would be excluded from such offerings. The SEC believes that the proposed increase in the offering limitation would increase the flexibility of state securities regulators to set their own state offering limitations and to consider whether any additional requirements should be implemented at the state level. In addition, the SEC believes that the proposed changes “would facilitate state efforts to increase the efficiencies associated with the registration of securities offerings in multiple jurisdictions through regional coordinated review programs.”

CONCLUSION

The proposed amendments to Rule 147 and Rule 504 represent the SEC’s first efforts since the enactment of the JOBS Act to address, through rulemaking, some of the other areas of concern for small company capital-raising that were not specified in the JOBS Act. Rather than utilizing preemption of state laws, as was done in Regulation A and Regulation Crowdfunding, the SEC’s proposed amendments recognize the role of state regulation and seek to utilize that regulation as a basis for exempting smaller offerings at the federal level. The proposals further recognize the work of the states in adopting their own crowdfunding exemptions and in coordinating blue sky review efforts.

Contact:

David M. Lynn
(202) 887-1563
dlynn@mofo.com

Anna T. Pinedo
(212) 468-8179
apinedo@mofo.com

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Summary Chart of Exempt Offering Alternatives

Below we provide a summary comparison of various securities exemptions.

Type of Offering	Dollar Limit	Manner of Offering	Issuer and Investor Requirements	Filing Requirement	Restriction on Resale	Blue Sky Exemption
Section 3(a)(11)	None.	No limitation other than to maintain intrastate character of offering.	Issuer and investors must be resident in state. No limitation on number.	None.	Rests within the state (generally a 9-month period for resales within state pursuant to Rule 147).	Need to comply with state blue sky laws by registration or state exemption.
Section 4(a)(2)	None.	No general solicitation or general advertising.	Investors must meet sophistication and access to information test so as not to need protection of registration.	None.	Restricted securities.	Need to comply with state blue sky laws.
Rule 504 Regulation D	\$1 million within prior 12 months.	No general solicitation or general advertising unless registered in a state requiring use of a substantive disclosure document or sold under state exemption for sales to accredited investors with general solicitation.	Available to non-reporting companies only that are not investment companies or blank check companies.	File Form D with the Commission not later than 15 days after first sale. Filing not a condition of the exemption.	Restricted unless registered in a state requiring use of a substantive disclosure document or sold under state exemption for sale to accredited investors with general solicitation.	Need to comply with state blue sky laws by registration or state exemption.
Rule 505 Regulation D	\$5 million within prior 12 months	No general solicitation or advertising.	Unlimited accredited investors and 35 non-accredited investors.	File Form D with the Commission not later than 15 days after first sale. Filing not a condition of the exemption.	Restricted securities.	Need to comply with state blue sky laws.
Rule 506(b)	None.	No general solicitation or general advertising under Rule 506(b).	Unlimited number of accredited investors and 35 non-accredited investors that are sophisticated.	File Form D with SEC not later than 15 days after first sale.	Restricted securities.	No need to comply with state blue sky laws.

Rule 506(c)	None.	General solicitation permitted, provided that all purchasers are accredited investors.	Under Rule 506(c), all purchasers must be accredited investors. Issuer must take reasonable steps to verify accredited investor status.	File Form D with the SEC not later than 15 days after first sale.	Restricted securities.	No need to comply with state blue sky laws.
Tier 1 Regulation A	\$20 million within prior 12 months, but no more than \$6 million by selling security holders.	“Testing the waters” permitted before and after filing Form 1-A. Sales permitted after Form 1-A qualified.	Eligible issuer No investor requirement.	File test-the-waters documents, Form 1-A, any sales material and report of sales and use of proceeds with the SEC.	Not restricted securities.	Subject to state blue sky laws regarding pre-offering review, filing, and anti-fraud.
Tier 2 Regulation A	\$50 million within the prior 12 months, but no more than \$15 million by selling security holders.	“Testing the waters” permitted before and after filing Form 1-A. Sales permitted after Form 1-A qualified.	Eligible issuer No investor requirement; however, investors who are natural persons and are not accredited investors are subject to an investment limit.	File test-the-waters documents, Form 1-A, any sales material and report of sales and use of proceeds with the SEC. Issuer subject to ongoing reporting requirements.	Not restricted securities.	Not subject to state blue sky laws regarding pre-offering review; however, subject to state blue sky filing and anti-fraud requirements.
Regulation Crowdfunding	Up to \$1 million in a 12-month period.	Offering must be made solely through a platform.	Issuers that are not reporting companies, not funds, and not subject to disqualification.	Requires the preparation of a Form C, which resembles a Form 1-A.	Securities sold in an offering are subject to certain transfer restrictions for one year.	No need to comply with state blue sky laws.