The JOBS Act and Advertising in Rule 506 Offerings

As you may know, President Obama signed the "Jumpstart Our Business Startups Act" (the JOBS Act) on April 5. This bill will make it substantially easier for companies to raise money although key provisions do not take effect immediately.

Two parts of the Act that will be important for companies using private placement offerings to raise money are the provisions allowing crowdfunding and the provisions relaxing restrictions on Rule 506 offerings. Neither will be available, though, until the Securities & Exchange Commission (SEC) issues regulations for both. The SEC has 90 days to issue the regulations for Rule 506 offerings and 270 days to issue regulations for the crowdfunding offerings. This email/post will deal with the Rule 506 provisions of the Act.

The big change is that public advertising is allowed, although then all investors must be accredited investors – no non-accredited but sophisticated investors are allowed. (See Section 201(a)(1) and (b).) The relatively high requirements for an accredited investor remain the same.

Basically, an accredited investor is: 1) Any individual whose net worth, or joint net worth with his/her spouse, exceeds \$1,000,000 excluding the primary residence; or 2) Any individual who either had income in excess of \$200,000 in each of the two last years or joint income with his/her spouse in excess of \$300,000 in those years and is reasonably expected to have the same income level in the current year; or 3) Any organization with total assets in excess of \$5,000,000 not formed for the purpose of acquiring the investment; or 4) Any organization in which each of the owners is an accredited investor.

Companies will have to decide whether public advertising will be worth giving up sophisticated investors who are not accredited. Presumably there will be a large number of companies publicly advertising for accredited investors. That means that some companies may prefer not to advertise publicly and rely instead on personal connections in order to have both accredited and sophisticated investors. It also is not clear what restrictions the SEC will put on the advertising; it may, for example, decide to restrict advertising to the brief "tombstone" ads allowed in California 25102(n) offerings and Model Accredited Investor Exemption offerings.

The JOBS Act also allows those who are not licensed as securities brokers to maintain "a platform or mechanism that permits the offer, sale, purchase, or negotiation of ...securities, or permits general solicitations, general advertisements, or similar or related activities by issuers of such securities, whether online, in person, or through any other means..." (Section 201(c).) Obviously this is designed to let Internet businesses provide lists of companies' offerings, presumably for a fee. In addition, this may confirm the use of exchanges where securities of a company can be traded after they are originally issued

even though those securities are not listed on an official stock exchange. It can make it easier for a company to sell securities if investors feel they have a way to sell their interests later

Further, right now securities generally can only be sold by management of the offering company or persons licensed as securities brokers. The JOBS Act allows others (let's call them "Affiliates") to be involved as well. It does not, though, allow the use of "finders" (non-brokers who are compensated on a performance basis for brining in investors) the way that a single-state offering may allow. (California law allows finders, for example.) These "Affiliates" may not receive "compensation in connection with the purchase or sale of such security" but may be compensated for "ancillary services" so long as they do not provide advice to the issuer or investors, do not negotiate the price of the securities and do not require the use of their own documents.

Of course, no one yet knows what the regulations that the SEC will adopt will look. Those regulations may have a substantial effect on the public advertising and "Affiliates" provisions.

-Bruce E. Methven