

Using the Reg. S Exemption for Foreign Investors

Foreign investors in U.S. companies can be handled one of two ways. One way to deal with non-U.S. investors is to treat them exactly like U.S. investors. Another option, though, is to use federal Regulation S with foreign investors.

Using Reg. S is useful when the issuer does not want to be limited by the restrictions of Rule 506. With a Rule 506 offering all investors must be either accredited or sophisticated, and there is a limit of 35 non-accredited investors. Offerings made pursuant to Reg. S do not have to meet either of those requirements. In short, there are no investor requirements and no limit on the number of investors.

To qualify for Reg. S, the offer and sale must be made in an "offshore transaction", meaning that the offer and sale cannot be made within the United States – even though the issuer itself is in the U.S. The offer and sale must be made only to foreign investors, meaning those who are not U.S. citizens, who do not reside in the U.S. and who are not in the United States at the time of the offer and sale.

No "directed selling efforts" can be made in the United States in connection with the offering to foreign investors. While emails and phone calls can be made to foreign investors who are not in the U.S., the SEC's position is that any Internet selling efforts must 1) include a prominent disclaimer saying that the offering is only for foreign residents, 2) the offeror's procedures must reasonably ensure that none of the securities in the offshore offering are purchased by U.S. persons and 3) access to the Internet material must be allowed only by password and only after the foreign person has shown that they are not a U.S. person. To be safe, responses to an investor questionnaire should be reviewed before providing a password.

In addition, as part of any sale each foreign investor must sign a certificate declaring that he/she/it is a foreign person and is not acquiring the securities for the benefit of any U.S. person. Further, the certificate must state that the securities will not be sold back into the U.S. unless in compliance with U.S. securities laws, and a legend stating this must be placed on the stock or other certificate. Finally, the issuer is required, either by contract or a provision in its bylaws, articles, charter or comparable document, to refuse to register any transfer of the securities not made in accordance with U.S. law.

Despite these restrictions, a separate Rule 506 offering can be made to U.S. investors that overlaps the offering to foreign investors. In other words, the usual integration rules do not apply to the two offers. The two offerings must be kept separate, but the materials for each may be very similar, requiring only the differences discussed above.

--Bruce E. Methven

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