TroyGould ATTORNEYS

Client Alert

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SEC Small Business Initiatives Update

In a series of initiatives earlier this year, the Securities and Exchange Commission (SEC) has sought to facilitate capital formation and reduce the SEC regulatory burden on small businesses.

First, on June 26, 2007, the SEC proposed to revise the eligibility requirements of Form S-3 and Form F-3, the SEC's short-form registration statements, to allow domestic and foreign issuers to conduct primary securities offerings on these forms without regard to the size of their public float, so long as they satisfy the other eligibility requirements of the respective form *and do not sell more than the equivalent of 20% of their public float in primary offerings pursuant to the new instructions on these forms over any period of 12 calendar months*. The proposal would not extend to shell companies, however, which would be prohibited from using Form S-3 and Form F-3 for primary offerings until 12 calendar months after they cease being shell companies.

On July 5, 2007, the SEC proposed changes to Rule 144 under the Securities Act of 1933, which creates a safe harbor for the sale of securities under the exemption set forth in Section 4(1) of the Securities Act. The SEC proposed a shortened six-month holding period requirement under Rule 144 for "restricted securities" of companies that are subject to the reporting requirements of the Securities Exchange Act of 1934. Restricted securities of companies that are not subject to the Exchange Act reporting requirements would continue to be subject to the current one-year holding period prior to any public resale.

The SEC also proposed to substantially reduce the restrictions on the resale of securities by non-affiliates, and to amend Securities Act Rule 145, which establishes resale limitations on certain persons who acquire securities in business combination transactions, to eliminate the presumptive underwriter position in Rule 145(c), except for transactions involving a shell company. The proposals are intended to increase the liquidity of privately sold securities and decrease the cost of capital for all companies (for example, by reducing the discount for restricted securities sold in PIPE transactions). Importantly, the proposal also would permit "tacking" of the holding period of securities issued in exchange for outstanding options, warrants and similar instruments (even where the original instrument does not provide for such an exchange), as long as no new consideration is given in connection with the exchange.

On July 19, 2007, the SEC proposed amendments to its rules relating to disclosure and reporting requirements for smaller companies under the Securities Act of 1933 and the Securities Exchange Act of 1934 to extend the benefits of the current optional disclosure and reporting requirements for small companies to a much larger group of companies. The proposals would allow companies with a public float of less than $75 million to qualify for the smaller company requirements, up from $25 million for most companies today. The proposals also would combine for most purposes the "small business issuer" and "non-accelerated filer" categories of smaller companies into a single category of

"smaller reporting companies." The proposals would maintain the current disclosure requirements for smaller companies contained in Regulation S-B, but integrate them into Regulation S-K, which governs the SEC disclosure requirements for other issuers.

On July 25, 2007, the SEC approved PCAOB Auditing Standard No. 5 regarding audits of internal control over financial reporting. While the new Auditing Standard applies to all reporting companies, it is specifically intended to reduce costs for small public companies by making Section 404 audits and management evaluations more "scalable" to company size and complexity. Under the new standard, the auditor can appropriately reduce the amount of internal control testing for audits of smaller and less complex companies.

On August 3, 2007, the SEC proposed several revisions to SEC Regulation D that, in general, would liberalize the regulation's private placement requirements. For example, the proposal would shorten from six months to 90 days the presumptive integration period for private placements. For more on this specific proposal, see SEC Proposes Changes to Regulation D's Private Placement Requirements.

The public comment periods on all of these proposals have now passed, and we would expect the proposals to soon be adopted by the SEC.