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LEGAL ALERT

April 6, 2012

JOBS Act to Make It Easier and Less Burdensome to Raise Capital in Securities Offerings

On April 5, 2012, President Obama signed the Jumpstart Our Business Startups Act (JOBS Act) into law.[1] The JOBS Act is intended to make it easier and less burdensome for companies to raise capital through securities offerings, including IPOs and private offerings. Some of the JOBS Act's provisions became effective immediately, while other provisions require rulemaking by the SEC under deadlines that vary from 90 to 270 days after enactment of the law. Appendix A to this legal alert contains a chart that sets forth the effective dates or rulemaking deadlines for the various provisions of the JOBS Act.

Overview

- Effective upon enactment of the JOBS Act, a new category of companies – "emerging growth companies" – will be able to take advantage of relaxed and less burdensome SEC rules in connection with their IPOs and subsequent SEC disclosure obligations for a period of up to five years after their IPOs.
- The prohibitions on general solicitation and general advertising in connection with Rule 506 offerings solely to "accredited investors" and Rule 144A offerings to "qualified institutional buyers" will be eliminated by SEC rulemaking within 90 days after the date of the enactment of the JOBS Act.
- Provisions permitting "crowdfunding" (which is a method of capital formation involving the solicitation of very small investment amounts from individual investors via social media or internet platforms) that will allow businesses to raise up to $1 million without registration under the Securities Act of 1933 (Securities Act) will be required to be put in place by SEC rulemaking within 270 days of the enactment of the JOBS Act.
- The offering amount limit for a new Regulation A-styled exemption will be $50 million upon the completion of SEC rulemaking that has no set deadline under the JOBS Act.
- Effective upon enactment of the JOBS Act, the Section 12(g) registration threshold under the Securities Exchange Act of 1934 (Exchange Act) is increased to either 2,000 record holders or 500 record holders who are non-accredited investors.

Initial Public Offerings

The JOBS Act eases regulatory requirements in connection with IPOs by companies that qualify as "emerging growth companies" and also reduces their SEC disclosure obligations for up to five years following the completion of their IPOs. An "emerging growth company" is defined as an issuer that had less than $1 billion in gross revenues during its most recently completed fiscal year and completed its IPO on or after December 8, 2011. An issuer will retain its status as an emerging growth company following

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[1] Jumpstart Our Business Startups Act of 2012, H.R. 3606, 112th Cong. (2012).

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the completion of its IPO until the earliest of: (i) the last day of the fiscal year in which the issuer had total annual gross revenues of $1 billion or more; (ii) the last day of the fiscal year following the five-year anniversary of the date of its IPO; (iii) the date on which the issuer has issued more than $1 billion in non-convertible debt in the previous three-year period; or (iv) the date on which the issuer is deemed a "large accelerated filer."[2]

An issuer that qualifies as an emerging growth company will be able to take advantage of the following relaxed rules in connection with its IPO and/or the reports it will be required to file with the SEC subsequent to its IPO:

- **Reduced Audited Financial Statement and MD&A Disclosure Requirements** – An emerging growth company will only be required to include two years (as opposed to three years) of audited financial statements in the registration statement for its IPO and will not be required to provide selected financial data or MD&A disclosure in the registration statement for any period prior to the earliest audited period presented in the registration statement. These same relaxed rules apply to the periodic reports that the emerging growth company will be required to file with the SEC subsequent to the completion of its IPO.

- **Exemption from Auditor Attestation on Internal Control over Financial Reporting –** An emerging growth company will not be subject to the requirement under Section 404(b) of the Sarbanes-Oxley Act of 2002 that its independent public accounting firm attest to its internal control over financial reporting. Prior to the enactment of the JOBS Act, an emerging growth company was required to include an audit report from its independent public accounting firm on its internal control over financial reporting in the second annual report on Form 10-K that it filed with the SEC subsequent to its IPO, to the extent that the market value of its common equity held by non-affiliates was $75 million or more.

- **Reduced Executive Compensation Disclosure** – An emerging growth company will be permitted to only include in its SEC filings the scaled disclosures on executive compensation required by "smaller reporting companies" under the SEC's rules. As a result, an emerging growth company may (i) omit the Compensation Discussion and Analysis, (ii) provide the Summary Compensation Table for two rather than three years, (iii) provide compensation information for three named executive officers rather than five, and (iv) omit most of the compensation tables that supplement the information contained in the Summary Compensation Table.

  In addition, an emerging growth company will be exempt from Dodd-Frank Act requirements, which remain subject to future SEC rulemaking, to provide a comparison of executive pay to the company's financial performance and to the median pay of all other employees.

  Furthermore, an emerging growth company will be exempt from the requirements to seek shareholder approval of an advisory vote on its executive compensation arrangements.

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[2] A "large accelerated filer" is an issuer that meets the following conditions at the end of its fiscal year: (1) had an aggregate worldwide market value of voting and non-voting common equity held by its non-affiliates of $700 million or more, as of the last business date of the issuer's most recently completed fiscal quarter; (2) has been subject to the requirements of Sections 13(a) and 15(d) of the Exchange Act for the last 12 calendar months; (3) has filed at least one annual report on Form 10-K with the SEC; and (4) is not eligible to use the requirements for smaller reporting companies for its annual reports on Form 10-K and quarterly reports on Form 10-Q.

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- **Exemption from New or Revised Accounting Standards and Certain PCAOB Rules –** Emerging growth companies do not have to comply with new or revised accounting standards until the date that these standards apply to private companies.

  In addition, emerging growth companies do not have to comply with any rules adopted in the future by the Public Company Accounting Oversight Board (PCAOB) requiring mandatory audit firm rotation or a supplement to the report of their independent registered public accounting firms to provide additional information about the audit and the financial statements of the emerging growth company. The PCAOB issued concept releases in 2011 that sought comment on these two provisions.

- **Confidential Submission of Initial Public Offering Registration Statement –** An emerging growth company can submit a draft registration statement to be used in connection with its IPO to the SEC for confidential review. These confidential submissions will be exempt from the Freedom of Information Act, but will have to be publicly filed with the SEC at least 21 days before the road show for the IPO.

- **"Testing the Waters" Provision** – Emerging growth companies and persons acting on their behalf will be able to make oral and written offers to sell their securities to "qualified institutional investors," as such term is defined in Rule 144A under the Securities Act, and institutional "accredited investors," as such term is defined in Rule 501 of Regulation D under the Securities Act, before the filing, and during the pendency of the SEC review of their registration statements. Prior to the JOBS Act, no oral or written offers to sell securities could be made prior to the filing of the IPO registration statement with the SEC, and no written offers, other than by use of the Section 10 prospectus included in the registration statement or certain free writing prospectuses, could be made subsequent to the filing of the IPO registration statement with the SEC.

- **Research Reports –** Under the JOBS Act, research reports distributed by broker-dealers, including the underwriter of the IPO, for an emerging growth company that is proposing to file or has filed a registration statement does not constitute an offer to sell a security for purposes of the registration requirements under Section 5 of the Securities Act. Further, the JOBS Act prevents the SEC or a registered national securities association from restricting which members of a broker-dealer may arrange for securities analyst communications with potential investors. Additionally, the JOBS Act allows for securities analysts to participate in meetings with the management of an emerging growth company where broker-dealer personnel who are not acting in a securities analyst role are present.

- **Ability to Opt-Out of Rules Applicable to Emerging Growth Companies** – An emerging growth company may choose to "opt-out" of the various cost-saving exemptions and scaled disclosure obligations and instead comply with the requirements applicable to non-emerging growth companies. However, an emerging growth company must choose whether it will avail itself of the exemption regarding the extension of time to comply with new or revised accounting standards in connection with the first filing it makes with the SEC.

Private and Exempt Offerings

In addition to the IPO provisions that are only applicable to emerging growth companies, the JOBS Act directs the SEC to relax certain restrictions on private and exempt offerings, and the related requirement of when companies, investment vehicles, and other entities must subject themselves to the periodic and current reporting requirements of the Exchange Act.

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- **General Solicitation in Connection with Rule 506 and Rule 144A Offerings** – Rule 506 of Regulation D provides a safe harbor from the registration requirements of Section 5 of the Securities Act under which an operating company or investment vehicle can conduct a private placement with no limitation as to dollar amount of the offering. Rule 144A is a safe harbor exemption from the registration requirements of Section 5 of the Securities Act for certain offers and sales of qualifying securities to "qualified institutional buyers" by certain persons other than the issuer of the securities. An issuer wishing to rely on Rule 506 in connection with the sale of its securities, or a person other than the issuer, including an investment banking firm, wishing to rely on Rule 144A in connection with the resale of securities, currently may not offer such securities for sale by any form of general solicitation or advertising.

  The SEC will be required to modify Rule 506 to permit general solicitation and advertising in connection with offerings under Rule 506 so long as all purchasers in such offerings are "accredited investors." Likewise, the SEC will be required to modify Rule 144A to permit general solicitation and advertising in connection with offerings under Rule 144A so long as all purchasers in such offerings are "qualified institutional buyers."

- **Creation of New Regulation A-Styled Exemption –** Regulation A currently provides an exemption from registration for transactions by issuers of up to $5 million in any 12-month period. Regulation A may not be relied upon by an issuer that is (i) subject to reporting requirements of Section 13 or Section 15(d) of the Exchange Act; (ii) an investment company registered or required to be registered under the Investment Company Act of 1940 (Investment Company Act), or (iii) a development stage company that either has no specific business plan or purpose or has indicated that its business is to engage in a merger or acquisition with an unidentified company or companies. If an issuer chooses to rely on Regulation A, it will be required to file an offering statement, consisting of a notification, offering circular and exhibits, with the SEC for review. As a practical matter, Regulation A offerings are more akin to registered offerings than exempt offerings.

  The JOBS Act amends the Securities Act to create a Regulation A-like exemption from the registration requirements under the Securities Act with the following attributes:

  - Permits the aggregate offering threshold of up to $50 million in any 12-month period of equity securities, debt securities or debt securities convertible or exchangeable to equity securities;
  - Permits issuers to "test the waters" by soliciting interest in the offering prior to filing any offering statement with the SEC, on such terms and conditions as may be determined by the SEC;
  - Will require issuers to annually file audited financial statements with the SEC and grants the SEC additional authority to require issuers relying on the new exemption to make other periodic disclosures;
  - Provides that securities can be offered and sold publicly and will not be considered "restricted securities" for purposes of Rule 144 under the Securities Act;
  - Provides that certain "bad actors" will not be eligible to rely on the new exemption;
  - Provides that the civil liability provision in Section 12(a)(2) of the Securities Act will apply to any person offering or selling securities pursuant to the new exemption; and

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- Preempts the authority of state securities commissioners to require registration and establish offering requirements for certain offerings made pursuant to the new exemption.

- **Crowdfunding Exemption –** The JOBS Act adds a transactional exemption to Section 4 of the Securities Act for "crowdfunding" which allows issuers to raise up to $1 million without having to comply with Section 5 of the Securities Act. Crowdfunding generally involves raising funds for a common cause or venture through the use of social media to obtain small contributions from many individuals. The crowdfunding transaction must be conducted through a broker or funding portal[3] which complies with certain requirements.

  To use the crowdfunding exemption, an issuer must have issued less than $1 million of its securities during the 12-month period prior to the transaction. The crowdfunding exemption is only available to non-SEC reporting issuers which are organized in the U.S. and are not investment companies or exempted investment companies under the Investment Company Act.

  The JOBS Act limits the amount of money that individuals can invest with a company for the 12-month period prior to the crowdfunding transaction. Investors with an annual income or net worth below $100,000 are limited to investing the greater of $2,000 or 5% of the investor's annual income or net worth in the issuer's securities. Investors with annual income or net worth of $100,000 are limited to investing up to 10% of that investor's annual income or net worth in the issuer's securities, up to a $100,000 maximum.

  Issuers that participate in crowdfunding will required to file with the SEC and disclose to potential investors: (1) the issuer's name, legal status, physical address and website; (2) the names of the directors, officers and shareholders with more than 20% ownership interest; (3) a description of the issuer and the issuer's anticipated business plan; (4) a description of the issuer's financial condition; (5) the intended purpose for the proceeds; (6) the target amount of the offering and the deadline to reach that amount; (7) the price or method of calculating the price of the securities to the public; (8) a description of the ownership and capital structure of the issuer; and (9) any other information that the SEC may require by rule to protect investors.

  With the exception of notices to direct investors to the broker or funding portal for the crowdfunding offering, issuers are prohibited from advertising any terms of an offering to investors. Issuers that rely on the crowdfunding exemption will be required to file their financial statements and disclosures about the results of operations with the SEC and provide them to investors on an annual basis.

  Crowdfunding transactions must be completed through a broker or funding portal that is registered with the SEC and an applicable self-regulatory organization. As long as a funding portal remains subject to SEC authority, is a member of a national securities association, and meets the requirements that the SEC prescribes, the funding portal need not register as a broker-dealer. However, a funding portal must be a member of a registered national securities association and is still subject to SEC examination, enforcement, rulemakings and any other requirements the SEC deems appropriate.

[3] As defined in the JOBS Act, a "funding portal" means any person acting as an intermediary in a transaction involving the offer or sale of securities for the account of others, solely pursuant to section 4(6) of the Securities Act, that does not (A) offer investment advice or recommendations; (B) solicit purchases, sales or offers to buy the securities offered or displayed on its website or portal; (C) compensate employees, agents or other persons for such solicitation or based on the sale of securities displayed or referenced on its website or portal; (D) hold, manage, possess or otherwise handle investor funds or securities; or (E) engage in such other activities as the Commission, by rule, determines appropriate.

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As an intermediary, a broker or funding portal must disclose to investors the risks of the investment as well as any investor education materials that the SEC may require. This intermediary must ensure that the investor reviews the investor-education information and understands the risks, illiquidity, extent of possible loss and nature of the company in which the investor is purchasing securities. The intermediary must also take measures to reduce the risk of fraud with the transaction by completing a background check on the officers, directors and any shareholders with more than a 20% ownership interest. The intermediary must deliver any information received from the issuer to the SEC not later than 21 days prior to the first day on which securities will be sold. The intermediary must also ensure that the aggregate amount of capital raised is equal to or greater than the target offering amount and that investors are allowed to cancel their commitments to invest, and that individual investors do not exceed their respective maximum allowed investments with all issuers, and that the privacy of any investor information collected is protected. Intermediaries are prohibited from compensating promoters, finders or lead generators and must prohibit any director, officer, or partner of the intermediary from having a financial interest in the issuer.

Investors that purchase securities offered pursuant to the crowdfunding exemption have a private right of action against the issuer for rescission based on material misstatements or omissions in connection therewith. For liability purposes, directors, partners, principal executive officers, principal financial and accounting officers, and any person who offers or sells the security in the offering is considered an issuer. An investor that purchases securities pursuant to the crowdfunding exemption may only resell those securities to the issuer, an accredited investor, as part of an SEC registered offering, to a family member, or in connection with death or divorce for one year after the purchase date of securities issued pursuant to the crowdfunding exemption.

While the JOBS Act preempts state securities laws concerning registration, documentation and offering requirements for securities issued pursuant to the crowdfunding exemption, it does not limit or impact states' enforcement actions concerning fraud, deceit or unlawful conduct of an issuer, funding portal, or any other person or entity using the exemption.

- **Increased Threshold Prior to Being Subjected to Periodic Reporting Requirements –** In an effort to delay the applicability of the Exchange Act's registration requirements for private companies and investment funds, the JOBS Act increases the shareholder threshold from securities "held of record" by 500 shareholders to either 2,000 shareholders or 500 non-accredited individual investors. The JOBS Act exempts shareholders who have received their securities pursuant to an employee compensation plan from the "held of record" determination.

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Appendix A

Section	Provisions	Rulemaking or Report Required	Effective Date
Emerging Growth Companies (EGCs)	Eligibility Requirements	None	Effective immediately upon enactment of the JOBS Act.
	Disclosure Obligations and Available Exemptions for EGCs	None	Effective immediately upon enactment of the JOBS Act.
	Research Reports and Communications about EGCs	None	Effective immediately upon enactment of the JOBS Act.
	Submission of Draft Registration Statements by EGCs	None	Effective immediately upon enactment of the JOBS Act.
	SEC Study and Report of Tick Size	Study shall examine the impact that decimalization has had on the number of IPOs since its implementation relative to the period before its implementation, and also shall examine the impact that this change has had on liquidity for small and middle capitalization company securities.	No later than 90 days from the enactment of the JOBS Act, the SEC must submit a report of its findings to Congress. NOTE: If the SEC determines that the securities of EGCs should be quoted and traded using a minimum increment greater than \$0.01, the SEC may by rule designate a minimum increment between \$0.01 and \$0.10 – within 180 days of submitting the report to Congress.
	SEC Review of Regulation S-K	Review shall examine whether there is a way to simplify the disclosure obligations and reduce the costs and other burdens for issuers that are not EGCs.	No later than 180 days after the enactment of the JOBS Act, the SEC must submit a report of the review of Regulation S-K to Congress. The report must provide specific recommendations on how to streamline the registration process.
Crowdfunding	All crowdfunding provisions	The SEC is required to create rules that it deems necessary to enact the requirements of the crowdfunding provisions.	No later than 270 days after the enactment of the JOBS Act.

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Section	Provisions	Rulemaking or Report Required	Effective Date
Rule 506 of Regulation D	General solicitation and advertising when the purchaser is an accredited investor.	The SEC is required to revise its rules to allow for general solicitation and advertising as long as the purchasers are accredited investors. The rules shall require the issuer to take reasonable steps to determine whether the purchasers are accredited investors. The SEC will provide methods to make this determination.	Rulemaking is required no later than 90 days after the date of the enactment of the JOBS Act.
Rule 144A	General solicitation and advertising when the purchaser is a qualified institutional buyer.	The SEC is required to revise its rules to allow for general solicitation and advertising as long as the seller reasonably believes that the purchasers are qualified institutional buyers.	Rulemaking is required no later than 90 days after the date of the enactment of the JOBS Act.
New Regulation A-Styled Exemption	Offering threshold to $50 million in any 12-month period.	The SEC is required to revise Regulation A accordingly.	There is no deadline provided for this rulemaking.
	Study on the Impact on Blue Sky Laws on Regulation A Offerings	The Comptroller General is required to conduct a study on the impact of State laws regulating securities offerings made under Regulation A.	No later than 3 months after the date of the enactment of the JOBS Act, the Comptroller General must submit a report to Congress on its findings.
Threshold for Registration	Increase the Section 12(g) registration threshold under the Exchange Act to 2,000 record holders or 500 record holders who are not accredited investors.	None	Effective immediately upon enactment of the Act.
	The definition of held of record does not include securities held by persons who received the securities pursuant to a compensation plan in transactions exempt from the registration requirements of Section 5 of the Securities Act.	The SEC is required to revise the definition of “held of record.” The SEC is also required to provide safe harbor provisions that issuers can use to determine whether holders of their securities received the securities through a compensation plan.	There is no deadline provided for this rulemaking.
	Enforcement Study	The SEC is required to determine whether new enforcement tools are needed to enforce the anti-evasion provision of Rule 12g5-1	The SEC is required to submit its recommendations under this study to Congress within 120 days after the date the JOBS Act is enacted.

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