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Securities Law Alert

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JOBS Act: New Law Facilitates Raising Capital

On April 5, 2012, the Jumpstart Our Business Startups Act of 2012, or JOBS Act, became law. The new law makes significant changes to how businesses can raise capital, among other changes described below:

- Eases IPO process and reporting requirements for emerging growth companies
- Reduces general solicitation and general advertising restrictions for certain private placements
- Creates new $50 million small public offering exemption
- Creates "crowdfunding" private placement exemption
- Increases the number of shareholders a private company may have without having to publicly report under the Exchange Act

Emerging Growth Companies

The JOBS Act implements measures relating to the IPO process and reporting requirements for a new category of issuer known as the "emerging growth company," or EGC. The new law defines an EGC as a company with annual gross revenues of less than $1 billion during its most recent fiscal year. A company can retain its EGC status for up to five years after going public depending on if it exceeds certain thresholds for annual revenue, market cap, and issuances of non-convertible debt.

During the IPO process, an EGC has reduced reporting and disclosure requirements and fewer restrictions on communications ahead of public offerings in order to "test the waters" before a contemplated offering. An EGC may also submit a draft of its registration statement for confidential, nonpublic review. Following an IPO, an EGC continues to have reduced reporting and disclosure requirements, including relief from auditor attestation of internal controls as required by Section 404(b) of the Sarbanes-Oxley Act of 2002.

Private Placements – Fewer Restrictions on General Solicitation and Advertising

By July 4, 2012, the SEC must revise Regulation D to allow general solicitation and general advertising for certain private placements of securities under Rule 506 and certain resales under Rule 144A. Depending on how the SEC revises its rules, this change could expand the ways companies seek investors for private offerings.

For example, in addition to loosening advertising and soliciting restrictions, the new law allows for online platforms to match companies with investors and exempts such platforms from broker-dealer registration if certain requirements are met. Furthermore, companies may now be able to advertise initial purchasers or placement agents in press releases announcing offerings. The implications of the law could affect how public and private offerings become integrated and whether multiple exemptions from registration of private placements can apply to a single issuer. At a minimum, issuers should revaluate how they identify accredited investors.

$50 Million Public Offering Exemption (Regulation A+)

The JOBS Act directs the SEC to create a new securities exemption to permit offerings of up to $50 million in any 12-month period. Before the JOBS Act, the securities laws gave the SEC authority to create a similar exemption, known as Regulation A (the small public offering exemption), but a Regulation A offering must be capped at $5 million and is not available to public companies. The $5 million cap is arguably one of the biggest disadvantages of a Regulation A offering.

Securities issued under the new $50 million exemption known as "Regulation A+" may be sold publicly and will not be considered restricted securities. The new exemption requires the SEC to issue implementing rules regarding delivery of the offering statement and other information about the issuer to investors. Issuers must file audited financial statements annually and may solicit interest in the offering before filing an offering statement, subject to additional rules to be set by the SEC. The JOBS Act does not set a deadline for this rulemaking.

For some issuers the new Regulation A+ could be a viable alternative for raising capital to an initial public offering or a Regulation D private placement.

Crowdfunding

The JOBS Act creates a new securities registration exemption known as "crowdfunding" that issuers can rely on to sell up to $1 million worth of securities to non-accredited investors as long as no individual investor invests more than:

a) $2,000 or 5% of the investor's annual income in any 12-month period (for investors with annual income or net worth less than $100,000); or

b) 10% of the investor's annual income or net worth up to $100,000 in any 12-month period (for investors with annual income or net worth in excess of $100,000).

The SEC has 270 days to enact the necessary rules to allow for crowdfunding. The securities may only be issued through a registered broker-dealer or "funding portal" over the internet that complies with additional requirements. The issuer has certain disclosure requirements during the offering process and following the offering.

Once the necessary SEC rules are in place, entrepreneurs and startups that do not typically have access to traditional venture capital will have the ability to raise money from a broad group of investors through the internet and social media.

Threshold for Exchange Act Registration

Currently, under Section 12(g) of the Securities Exchange Act of 1934, companies with more than $10 million in assets whose equity securities are held of record by more than 500 holders must file periodic reports with the SEC. The new law increases the holders of record threshold for most issues to either (i) 2,000 persons, or (ii) 500 persons who are not accredited investors. For banks and bank holding companies, the threshold number of record holders has been increased to 2,000 persons. Banks and bank holding companies can also now deregister and suspend Exchange Act reporting if the number of holders of record of a class of securities falls below 1,200 (increased from 300).

The impact of these changes would provide many issuers, especially banks and bank holding companies, with room to raise additional capital, without fear of triggering public company reporting requirements, and may also cause some banks to consider deregistration.

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