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THE JOBS ACT: NEW RULES FOR EMERGING GROWTH COMPANIES, PRIVATE PLACEMENTS AND "CROWDFUNDING"

On March 27, 2012, the Jumpstart Our Business Startups Act (the "JOBS Act") was sent to President Obama for signing, which is expected soon. According to the preamble for the legislation, the JOBS Act is intended to increase American job creation and stimulate economic growth by improving access to the public capital markets for a new category of issuer created by the JOBS Act -- the "emerging growth company." The JOBS Act also includes provisions that reduce restrictions for all companies (whether or not emerging growth companies) on exempt offerings under Regulation D and Rule 144A under the Securities Act of 1933 (the "Securities Act") and may facilitate the ability of companies to access capital without registration with the Securities and Exchange Commission (the "SEC"). Whether the legislation will achieve its purpose is an open question -- the JOBS Act met with criticism and skepticism by the SEC and many institutions, some believing the Act will not do much more than add costs, raise confusion and open the door to fraudulent behavior.[1] In this advisory we discuss the key elements of the JOBS Act as well as their implications for companies, investors and financial intermediaries.

"IPO ON-RAMP" FOR EMERGING GROWTH COMPANIES

The JOBS Act provides a number of significant regulatory changes for a new category of issuer - the "emerging growth company" -- which the JOBS Act defines as an issuer that has annual gross revenue of less than $1 billion during its most recently completed fiscal year.[2] Any issuer that made its first registered sale of common equity securities ("IPO") on or before December 8, 2011 would not be eligible to be treated as an emerging growth company.[3] An issuer that qualifies will continue to be eligible to treat itself as an emerging growth company until the earliest of:

- the first fiscal year after it has annual revenue in excess of $1 billion (as indexed for inflation every five years by the SEC);

[1] *See*, *e.g.*, Letter from SEC Chairman Mary Schapiro to Chairman Tim Johnson and Ranking Member Richard C. Shelby, Committee on Banking, Housing, and Urban Affairs, U.S. Senate ("Schapiro Letter"), dated March 13, 2012; Letter from Council of Institutional Investors to Senators Johnson and Shelby, dated March 1, 2012; Letter from AFSCME, Americans for Financial Reform, Chicago Consumer Coalition, *et al* to Senators Johnson and Shelby, dated March 5, 2012; Letter from AARP to Senate Majority Leader Harry Reid, dated March 7, 2012; and Letter from Representative John Sarbanes to Colleagues, dated March 7, 2012.

[2] It has been estimated that 98% of all companies that completed an IPO since 1970 would be emerging growth companies, calling into the question of whether "emerging" is an accurate term. *See generally* Letter from Representative John Sarbanes to Colleagues, dated March 7, 2012.

[3] As a result of this definition, most companies that are currently public cannot rely on the new classification. Unless the SEC amends the definition of an emerging growth company, it appears that a company that became public before December 8, 2011 only through a registration statement filed under the Securities Exchange Act of 1934 (the "Exchange Act") (*e.g.*, on a Form 10 or Form 20-F), as well as a company that prior to the same date had only registered offerings of securities other than common equity, could still become an emerging growth company, assuming it meets the revenue test. This would be because the company could engage in its first sale of registered common equity after the December 8, 2011 start date.

- the beginning of the sixth fiscal year after the first registered sale of its common equity securities in an IPO;
- the date upon which it has issued in excess of $1 billion of non-convertible debt during the previous three-year period; or
- the date on which it would be deemed to be a "large accelerated filer" under the Exchange Act, which the SEC defines as a company that has a public float of $700 million or more of common equity securities and has been filing SEC reports for at least one year.[4]

The changes in current securities laws that will apply to emerging growth companies are summarized below. How these changes will work in practice is somewhat unclear in a number of cases and, in any event, most of the changes are only loosely coordinated with existing SEC rules. For this reason, there are a number of issues posed by the legislation that may be difficult to advise on definitively until the SEC provides clarification either through rulemaking or interpretive guidance.

Changes to IPO Process

- **CONFIDENTIAL REVIEW.** Section 106 of the JOBS Act permits an emerging growth company to submit its IPO registration statement confidentially in draft form for SEC staff review. This option, historically available only to foreign issuers or upon pre-filing accommodations granted on a case by case basis, would allow an emerging growth company to commence the IPO process without publicly disclosing sensitive information and with the possibility of later discontinuing its IPO plans without the market being aware.[5] Notwithstanding the initial confidential treatment of a filing by an emerging growth company, Section 106 also requires that such a company publicly file the initial confidential submission (and all amendments) at least 21 days prior to the road show for the IPO.[6]

  We note that Groupon's recently-announced restatement of its first full quarterly results following its IPO, along with its need to change its accounting practices twice during the SEC staff's review of its initial registration statement, has led to increased focus on whether this confidential review provision of the JOBS Act will impair transparency for IPO investors. Supporters of the JOBS Act have indicated that the SEC could, in implementing regulations, require issuers to disclose the contents of their confidential filings when they register publicly with the SEC, which would likely be well in advance of the 21-day minimum disclosure period mandated by the JOBS Act.[7]

- **FINANCIAL INFORMATION.** Section 102 of the JOBS Act permits an emerging growth company to present only two years of audited financial statements in its IPO registration statement (rather

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[4] In 2005, the SEC estimated that 30% of public companies in 2004 would qualify under a definition that is nearly identical to the threshold at which a company no longer qualifies as an emerging growth company, *i.e.*, the threshold for becoming a "well-known seasoned issuer." *See* SEC Rel. No. 33-8591 (June 2005) ("In 2004, [well-known seasoned issuers] … represented approximately 30% of listed issuers …."). By negative implication, this estimate suggests that 70% of listed companies in 2004 could qualify as "emerging growth companies" if they were to conduct initial public offerings following the enactment of the JOBS Act.

[5] The SEC scaled back the confidential review process as it relates to foreign private issuers in December 2011. *See* SEC, Non-Public Submissions from Foreign Private Issuers, December 8, 2011, available at http://www.sec.gov/divisions/corpfin/internatl/nonpublicsubmissions.htm. SEC Chairman Mary Schapiro believes that allowing emerging growth companies to file registration statements confidentially will "hamper the staff's ability to provide effective reviews," "require significant resources for staff review of offerings that companies are not willing to make public and then abandon before making a public filing," and ultimately "adversely impact the IPO review program." *See* Schapiro Letter at 4.

[6] *See* Securities Act Rule 433(h)(4). Note that the broad definition of "road show" in Rule 433(h)(4) could encompass "test the waters" communications, as discussed below, if they involve company management. Absent clarification from the SEC on this point, an emerging growth company making a confidential filing of its draft IPO registration statement may need to have its management refrain from such communications with prospective investors, but could permit financial intermediaries, such as investment banks and other broker-dealers, to make such communications on its behalf.

[7] *See, e.g.,* Michael Rapoport, In Wake of Groupon Issues, Critics Wary of JOBS Act, WALL ST. J., April 2, 2012, at B1.

than the three years required of other larger companies); and in subsequent registration statements, it need not present selected financial data for any period prior to the earliest audited period presented in connection with its IPO registration statement.[8] An emerging growth company also is not required to comply with any new or revised financial accounting standard until the time that such standard applies to companies that are not "issuers" under the Sarbanes-Oxley Act of 2002 (*i.e.*, companies that are not public and that have not filed a registration statement with the SEC).

- **"TEST THE WATERS" COMMUNICATIONS.** Section 105(c) of the JOBS Act allows an emerging growth company (directly or through any person authorized to act on its behalf) to "test the waters" with potential investors that are qualified institutional buyers[9] or institutions that are accredited investors[10] to determine whether such investors would be interested in an offering prior to filing a registration statement. This would permit the emerging growth company to communicate either orally or in writing with qualified institutional buyers and institutional accredited investors both before and after filing the registration statement. In contrast to current SEC rules permitting "test the waters" activities, the JOBS Act does not require emerging growth companies to file materials they use to assess investor interest.[11]
- **RESEARCH REPORTS.** Under Section 105(a) of the JOBS Act, the publication or distribution by a broker-dealer of a research report about an emerging growth company that is the subject of a proposed registered public offering of common equity securities will not constitute an offer of securities, regardless of whether the report is issued before, during or after the offering and even if the broker-dealer is participating in the offering. It thereby creates a safe harbor for the issuance of research reports in advance of and during the registration period for such offerings, when such reports would previously have created a risk of an illegal offer (often referred to as "gun-jumping") or non-conforming prospectus. Section 105(d) also specifically eliminates, for IPOs of emerging growth companies, the existing quiet period imposed immediately after IPOs and the quiet period imposed prior to the expiration of lock-up periods (although it does not provide for elimination of the quiet period immediately after expiration of lock-ups).
- **COMMUNICATIONS AMONG RESEARCH ANALYSTS, INVESTORS AND MANAGEMENT.** Section 105(b) of the JOBS Act removes restrictions regarding who within a broker-dealer can arrange for communications between research analysts and investors in connection with IPOs by emerging growth companies, including by permitting investment bankers to be involved in those arrangements. Further, in connection with such an offering, it allows participation by a research analyst in communications with the emerging growth company's management where other representatives of the broker-dealer, including investment bankers, are also present. These provisions of the JOBS Act carve exceptions out from existing NASD and NYSE rules on research analyst independence.

  It is less clear what effect these JOBS Act provisions may have upon the 2003-04 federal court-ordered global research settlement.[12] This court-ordered settlement was amended in 2010 but remains in effect as to the broker-dealer firms party to it, including its substantial restrictions on

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[8] *See* JOBS Act § 102. A registration statement for an initial public offering (other than for a "smaller reporting company") currently is required to include two years of balance sheets as well as three years of income statements, statements of comprehensive income, changes in stockholders equity and cash flow statements. It is unclear from the legislation whether this provision reduces the number of balance sheets from two to one. We would expect the SEC to provide clarification on this point in future interpretive guidance regarding the JOBS Act.

[9] The term "qualified institutional buyer" is defined in Securities Act Rule 144A(a).

[10] The term "accredited investor" is defined in Section 2(a)(15) of the Securities Act and Rule 501(a) of Regulation D.

[11] Chairman Schapiro maintains that the lack of a requirement to file such materials would "result in uneven information for investors who see both the 'test the waters' materials and the prospectus compared to those who only see the prospectus," and could result in investors focusing on the "test the waters" materials rather than the prospectuses. *See* Schapiro Letter at 3.

[12] *See* SEC Fact Sheet on Global Analyst Research Settlements (Apr. 28, 2003).

the permitted content of communications between investment bankers and research analysts and the requirement that many of such communications be chaperoned by legal or compliance professionals.[13] The settlement also forms the basis of practice standards which a number of institutional investors require their securities firms (whether or not parties to the settlement) to follow. It is unclear whether the settlement (which the SEC has the power to supersede with new rules) could itself be deemed a "rule or regulation" modified by the JOBS Act provisions; moreover, the JOBS Act provisions do not appear to restrict institutional investors' ability to impose tighter practice standards upon securities firms with which they do business. The interaction of the provisions of the JOBS Act with existing NASD and NYSE rules, with the continuing terms of the global research settlement, and with the practice standards applied by institutional investors, will be complex and should be carefully examined in the context of specific facts.

Reduced Reporting Requirements

The JOBS Act allows an emerging growth company to make scaled disclosures and enjoy other relief from specific disclosure requirements during a five-year period following its IPO (except for shorter periods as noted below). Specifically, an emerging growth company is not required to:

- provide selected financial data for any period prior to the earliest audited period presented in connection with its IPO registration statement;[14]
- have an auditor attest to the quality and reliability of the company's internal control over financial reporting;[15]
- comply with any new or revised financial accounting standard until the time that such standard applies to companies that are not "issuers" under the Sarbanes-Oxley Act of 2002 (*i.e.*, companies that are not public and that have not filed a registration statement with the SEC);[16]
- provide "management's discussion and analysis of financial condition and results of operations" disclosures beyond the periods presented in the financial statements required for emerging growth companies;[17]
- comply with any Public Company Accounting Oversight Board ("PCAOB") rules requiring mandatory audit firm rotation or an auditor discussion and analysis;[18]
- comply with any additional rules adopted by the PCAOB after the enactment of the JOBS Act unless the SEC determines that the application of such additional rules is "necessary or appropriate in the public interest;"[19]
- hold a shareholder vote on executive compensation, including "say-on-pay" votes and votes on golden parachute compensation for at least three years following its IPO;[20]

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[13] *See* SEC Litigation Rel. No. 21457 (Mar. 19, 2010).
[14] JOBS Act § 102(b).
[15] *Id.* § 103. Under current SEC rules, a company that has completed an IPO already has two years before it is required to obtain an attestation from its independent auditor regarding its internal control over financial reporting. Further, the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the "Dodd-Frank Act") permanently exempted smaller public companies (generally those with less than $75 million in public common equity float) from this requirement. *See* § 989G(a) of the Dodd-Frank Act; Item 308(b) of Regulation S-K. This exemption covers approximately 60% of reporting companies. *See* Study and Recommendations on Section 404(b) of the Sarbanes-Oxley Act of 2002 For Issuers With Public Float Between $75 and $250 Million, SEC Office of the Chief Accountant (April, 2011), at 8-9, available at http://www.sec.gov/news/studies/2011/404bfloat-study.pdf.
[16] *Id.* § 102(b).
[17] *Id.* § 102(c).
[18] *Id.* § 104.
[19] *Id.* § 104.
[20] *Id.* § 102(a).

- prepare a "compensation discussion and analysis" section in its executive compensation disclosures, provide executive compensation disclosures regarding more than three named executive officers, include more than two years of compensation information in the summary compensation table or provide four of the six executive compensation tables required for larger companies;[21] or
- disclose certain executive compensation information that will otherwise be required under the Dodd-Frank Act, including a comparison of executive compensation to performance and median compensation.[22]

Under Section 107 of the JOBS Act, an emerging growth company may opt to forego any exemption provided to emerging growth companies. However, if it does avail itself of the extension of time to comply with new or revised financial accounting standards available to such companies, it must make such election at the time it must file its first registration statement, periodic report or other report under Section 13 of the Exchange Act and notify the SEC of such choice. Further, it may not select some standards to comply with, and not others, but must comply with all such standards.

SEC Review of Regulation S-K

Under Section 108 of the JOBS Act, Congress directs the SEC to conduct a review of Regulation S-K. This review must analyze the current registration requirements and determine how such requirements can be updated to modernize and simplify the registration process and reduce the costs and other burdens associated with these requirements, all as applied to emerging growth companies. The SEC must deliver a report of its review and recommendations to Congress within 180 days of enactment of the JOBS Act. This may result in benefits for all issuers, as the SEC may find it difficult to differentiate between improvements that will be good for emerging growth companies versus all other issuers.

OTHER PROVISIONS RELATED TO CAPITAL RAISING

In addition to the IPO on-ramp and other accommodations for emerging growth companies, the JOBS Act has other provisions intended to give companies (whether or not emerging growth companies) easier access to capital.

General Solicitation in Private Placements

Section 201(a) of the JOBS Act requires the SEC, within 90 days, to revise its rules relating to non-public offerings in two respects. First, the SEC must revise Rule 506 of Regulation D to provide that offers and sales of securities under this rule may be made through the use of general solicitation or advertising provided that all purchasers of the securities are accredited investors.[23] The legislation requires the SEC to adopt rules requiring the issuer to take "reasonable steps to verify" such

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[21] *Id.* § 102(c).
[22] *Id.* § 102(a).
[23] The term "accredited investor" is defined in Section 2(a)(15) of the Securities Act and Rule 501(a) of Regulation D. Earlier this year, the SEC's Advisory Committee on Small and Emerging Companies (the "Advisory Committee"), formed in 2011, recommended that the SEC relax or modify the restrictions on general solicitation and advertising in offerings under Rule 506 where securities are sold only to accredited investors. *See* Advisory Committee, Recommendation Regarding Relaxing or Modifying Restrictions on General Solicitation in Certain Private Offerings of Securities, dated January 6, 2012. Since its inception, the Advisory Committee has issued nine recommendations to the SEC, a number of which touch on provisions of the JOBS Act.

investors are accredited investors and to set forth the methods that would satisfy this standard of verification.[24]

Second, the SEC must amend Rule 144A to provide that securities sold under this rule may be offered to persons other than qualified institutional buyers, including through general solicitation or advertising, provided that the securities are sold only to persons that the seller and any person acting on behalf of the seller "reasonably believe" are qualified institutional buyers.[25]

What reasonable steps an issuer must take to verify accredited investor status or what the seller must do to have a reasonable belief that a purchaser is a qualified institutional buyer will be critical to how the relaxation on general solicitation and advertising in Rule 506 and Rule 144A offerings is used. The new "verification" obligation represents a potentially significant departure from current law and practice, which is based solely upon establishment of a reasonable belief as to the status of the purchaser. While the SEC is only required to address Rule 506's new verification standard, the SEC may find it sensible to align that standard with other standards under its existing rules.[26]

For Rule 506 placements, Section 201(b) expressly extends the loosened general solicitation and advertising rule to the term "public offering" as used in other areas of the Federal securities laws, which would, in particular, include the "private fund" exemptions under Sections 3(c)(1) and (7) of the Investment Company Act of 1940. Section 201 contains no corresponding provision for Rule 144A transactions, however, leaving it unclear whether Rule 144A offerings of "private fund" securities may permissibly involve general solicitation or advertising. It is possible that the SEC will clarify this point in its implementing rules.

Section 201(c) of the JOBS Act provides for a limited exemption to registration as a broker-dealer with respect to securities offered and sold under Rule 506. A person will not be required to register as a broker-dealer solely because (i) such person maintains a securities platform or mechanism that permits activities such as the offer and sale of securities or general solicitation or general advertising by issuers of such securities, (ii) such person (or an associated person) co-invests in such securities or (iii) such person (or an associated person) provides "ancillary services" (as defined) with respect to such securities, provided that, in any case, such person (and each person associated with that person):

- receives no compensation in connection with the purchase or sale of such securities;
- does not have possession of customer funds or securities in connection with the purchase or sale of the securities; and
- is not subject to a statutory disqualification (as defined in Exchange Act Section 3(a)(39)).

Crowdfunding

One of the most controversial aspects of the JOBS Act relates to "crowdfunding", which refers to the ability of a company to raise limited amounts of capital from a large pool of investors, including over

[24] Importantly, Section 201 does not affect the general standards for a private placement exempt under Section 4(2) of the Securities Act, for which general solicitation and general advertising have been seen as negative factors.
[25] The term "qualified institutional buyer" is defined in Securities Act Rule 144A(a).
[26] Under current SEC rules, (i) an accredited investor is a person who the issuer "reasonably believes" fits within the categories specified in Regulation D (*see* Securities Act Rule 501(a)), (ii) under Securities Act Rule 144A(d)(1), issuers must "reasonably believe" that a person is a qualified institutional buyer, and (iii) issuers must exercise "reasonable care" to assure that purchasers of securities sold under Regulation D are not underwriters (*see* Securities Act Rule 502(d)). Note also that in proposed rulemaking under Regulation D in 2007, the SEC used a "reasonable belief" standard in a proposed amendment that would have permitted general solicitation and advertising to "large accredited investors." *See* SEC Proposing Rel. No. 33-8828, Aug. 3, 2007, at 12.

the internet. Title III of the JOBS Act adds a new Section 4(6) to the Securities Act to allow a company to offer and sell $1 million of securities over a 12-month period without registration under the Securities Act. Notwithstanding the debate surrounding this new exemption, its prospects may be quite limited given its long list of conditions. This may be even more so given the new amendments to Rule 506 and the relatively limited number of conditions that apply to offerings under that rule.

CONDITIONS ON ISSUERS ENGAGING IN CROWDFUNDING. Exchange Act reporting companies, companies organized outside of the United States and investment companies are precluded from relying on the crowdfunding exemption. State registration, documentation and offering requirements that would otherwise apply to crowdfunding are preempted by the JOBS Act; however, such offerings remain subject to state enforcement actions for fraud, deceit or similar unlawful conduct.

CONDITIONS ON AMOUNTS RAISED IN CROWDFUNDING OFFERINGS. The aggregate amount sold to any one investor in a 12-month period cannot exceed:

- the greater of $2,000 or 5% of the annual income or net worth, as applicable, for an investor who has an annual income or a net worth less than $100,000, and
- 10% of the annual income or net worth, as applicable, for an investor who has an annual income or net worth of $100,000 or more, but not to exceed $100,000.

CONDITIONS ON CONDUCT OF CROWDFUNDING OFFERINGS. Companies engaging in crowdfunding under the JOBS Act must comply with a number of requirements, including the following:[27]

- **CONDUCT OFFERINGS THROUGH REGISTERED BROKERS OR REGISTERED FUNDING PORTALS.** Crowdfunding offerings must be conducted through either a registered broker or a funding portal that is registered with the SEC. A broker or funding portal that facilitates crowdfunding offerings also must register with any applicable self-regulatory organization. A broker that is registered with the SEC need not also register as a funding portal.
- **PROVIDE LIMITED DISCLOSURES TO INVESTORS.** A company engaging in a crowdfunding must provide limited disclosures about itself and the offering, including the following:
  - information about the company, its officers, directors and 20% shareholders;
  - description of the company's business and anticipated business plan;
  - limited financial information about the company ranging, depending on the size of the offering, from income tax returns and financial statements certified by the CEO to audited financial statements;[28]
  - description of the use of the proceeds from the offering;
  - target offering amount, price of the securities and method by which the price was determined;
  - description of the company's ownership and capital structure; and
  - such other information as may be required by the SEC.
- **RESTRICTED ADVERTISEMENTS.** A company engaging in a crowdfunding may not advertise the terms of the offering except for notices that direct investors to the broker or funding portal.

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[27] These provisions were enhanced in an amendment to the House version of the JOBS Act largely in response to concerns raised by SEC Chairman Mary Schapiro and investor and consumer protection advocates. *See* Schapiro Letter at 4-5.

[28] For an offering of less than $100,000, a company must provide income tax returns and financial statements that are certified by the CEO. For an offering of between $100,000 and $500,000, a company must provide financial statements that have been reviewed by an independent public accountant. For offerings of $500,000 or more, a company must provide audited financial statements.

- **PAYMENTS TO BROKERS AND CROWDFUNDING PORTALS.** A company engaging in a crowdfunding may not compensate brokers or funding portals unless it follows steps still to be determined by SEC rulemaking.
- **SEC REPORTS.** A company engaging in a crowdfunding must file with the SEC and provide to investors reports of the results of operations and financial statements to be determined by subsequent SEC rulemaking.
- **TRANSFER RESTRICTIONS.** Shares sold through a crowdfunding will be subject to a one year transfer restriction unless such shares are resold to the issuer, an accredited investor, a family member or as part of a registered offering.
- **LIABILITY.** Section 302(c) of the JOBS Act provides a private right of action against a company engaging in a crowdfunding based on material written or oral misstatements or omissions in connection with such offering. The legislation provides that any liability under this section will be "as if the liability were created under section 12(a)(2)" of the Securities Act.

CONDITIONS APPLICABLE TO BROKERS AND CROWDFUNDING PORTALS. In addition to registration with the SEC and self-regulatory organizations, brokers and funding portals engaging in crowdfunding under the JOBS Act as intermediaries must:[29]

- provide disclosures to be determined by the SEC through rulemaking, including disclosures related to risks and other investor education materials, and ensure that each investor reviews such information, affirms that the investor understands the risks, and answers questions demonstrating an understanding of such risks and an understanding of other matters as determined by the SEC;
- take measures to be established by the SEC to reduce the risk of fraud, including background checks on issuers' officers, directors and holders of more than 20% of the outstanding equity;
- not later than 21 days prior to the first day on which securities are sold, make available to the SEC and potential investors the information the issuer is required to provide to investors (described above under "Provide Limited Disclosures to Investors");
- only provide offering proceeds to the issuer once the aggregate capital raised from all investors is equal to or greater than the target offering amount;
- make efforts, as the SEC determines appropriate, to ensure that no investor exceeds the limit allowed to be purchased by a crowdfunding investor in a 12-month period;
- take steps to protect the privacy of information collected from investors;
- not compensate promoters, finders or lead generators for identifying potential investors; and
- prohibit its directors, officers or partners from having a financial interest in an issuer using its services.

Within 270 days after the enactment of the JOBS Act, the SEC is required to issue rules necessary to implement certain requirements with respect to intermediaries in crowdfunding transactions, as well as rules or regulations to establish disqualification provisions under which an issuer would not be eligible to utilize the crowdfunding exemption to registration based on disciplinary history.[30]

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[29] *See* JOBS Act § 302(b).

[30] Chairman Schapiro has said that she believes that this and other rulemakings required by the JOBS Act have time limits that are not achievable. She believes that 18 months would be more appropriate for rules of this magnitude. *See* Schapiro Letter at 5.

Expansion of Regulation A

Title IV of the JOBS Act requires the SEC to amend the registration exemption in Regulation A under the Securities Act to increase the amount of securities that can be issued over a 12-month period under such exemption from $5 million to $50 million.[31] The exemption requires an offering document to be filed with the SEC, but the information requirements are simpler than those required in registered offerings. In a Regulation A offering, for instance, the issuer may provide the disclosure in a question and answer format and "test the waters" for interest in its offering before it incurs the full expense of preparing the Regulation A offering document. Regulation A exempt offerings are not limited to particular types of investors, although there are "bad actor" disqualifications for offering participants, and the securities purchased are not transfer-restricted under the Securities Act.[32]

THRESHOLDS FOR PUBLIC COMPANY REPORTING

The JOBS Act amends the thresholds that trigger registration of classes of securities and resulting periodic and other reporting obligations under the Exchange Act. Specifically, the JOBS Act significantly increases the record holder threshold in Section 12(g) of the Exchange Act.[33] The changes to the public company reporting triggers are detailed in the following table:

	PRE-JOBS ACT	POST-JOBS ACT
REGISTRATION AND REPORTING TRIGGERS	Total assets exceeding $10 million *and* a class of equity securities held of record by 500 or more persons ■ "Held of record" means only persons identified as owners on the records of security holders maintained by the company, or on its behalf, in accordance with accepted practice[34]	Total assets exceeding $10 million *and* a class of equity securities held of record by either 2,000 or more persons or 500 or more persons who are not accredited investors[35] ■ "Held of record" excludes shareholders who received securities under an employee compensation plan in transactions exempted from Securities Act registration[36] ■ For banks and bank holding companies the 2,000 shareholders trigger does not include a limit on shareholders who are not accredited investors
REGISTRATION AND REPORTING TERMINATION	Registration can be terminated upon certification that the number of holders of record is reduced to less than 300 persons	Registration can be terminated upon certification that the number of holders of record is reduced to less than 300 persons, or in the case of a bank or bank holding company, 1,200 persons

[31] This expansion of Regulation A was recommended by the Advisory Committee, albeit with additional safeguards. *See* Advisory Committee, Recommendations Regarding Improving Access to the Public Markets for Small and Emerging Companies, dated February 1, 2012.
[32] Regulation A has not been widely used recently. For the fiscal year ended September 30, 2010, there were 25 initial Regulation A filings with the SEC and only seven of such offerings were qualified. *See* Testimony of Meredith Cross on Crowdfunding and Capital Formation Before the Subcommittee on TARP, Financial Services and Bailouts of Public and Private Programs of the House of Representatives, Committee on Oversight and Government Reform, Sept. 15, 2011. Increasing the maximum amount for Regulation A offerings may increase the use of the exemption and also lessen any appeal of the crowdfunding provisions of the JOBS Act.
[33] *See* JOBS Act Titles V and VI. These changes are effective immediately once the JOBS Act is signed. The SEC is required, however, to revise the definition of "held of record" to conform to the new requirements in Section 12(g) of the Exchange Act and to adopt related safe harbor provisions within one year of enactment of the JOBS Act.
[34] *See* Exchange Act Rule 12g5-1.
[35] The Advisory Committee recommended that, while further review was ongoing, the SEC implement an interim rule which would provide that registration would not be triggered until a company had a class of securities held by 1,000 or more holders of record or, in the case of a banking institution, 2,000 or more holders of record, with termination of registration allowed once the number of holders of record was less than 600 holders of record or, for a banking institution, 1,200 holders of record; in either case, the Advisory Committee recommended that employees subject to trading restrictions not be counted in determining whether the thresholds were met. *See* Advisory Committee, Recommendations Regarding Registration Requirements and Reporting Obligations under the Exchange Act, dated February 1, 2012.
[36] In addition, JOBS Act § 303 requires the SEC to exclude shareholders who have received securities in an exempt crowdfunding offering.

While these changes are intended to defer public company reporting burdens for a private company until it has more shareholders, this benefit will not be realized fully without increased administrative costs. At a minimum, to take full advantage of these changes, a company will need to maintain detailed records of its shareholders, including a record of which shareholders are accredited, "crowdfunders" and holders of securities issued by employee compensation plans in exempt offerings. Further, given that the status of shareholders will change over time, such a company will also have to keep its shareholder records updated for these three categories.

CONCLUSION

Despite its lofty goals, the JOBS Act seems an unlikely agent for job creation and economic growth. To be sure, some provisions, such as the loosening of restrictions on exempt offerings, could have important and lasting effects on capital raising. The benefits of other provisions, such as the relaxation of the rules regarding research reports and analysts, the increase in the threshold for registration under the Exchange Act and the new crowdfunding exemption, are less certain to benefit capital formation, much less job creation. In all events, however, since many potential benefits of the JOBS Act will hinge on subsequent rulemaking by the SEC, at a time when it continues to struggle under rulemaking burdens imposed by the Dodd-Frank Act, this case is far from closed.

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