

SECURITIES OFFERINGS

Title II of the JOBS Act: Are Reports of the Death of General Solicitation Premature?

Title II of the JOBS Act directs the Securities and Exchange Commission to amend exemptive safe harbors under the Securities Act of 1933 to permit the use of general solicitation to offer securities. Although this means that securities can be offered to anyone once the Commission amends these rules, there is a significant catch—only “accredited investors” or QIBs may buy the securities.

By Catherine T. Dixon

With the enactment on April 5, 2012, of the Jumpstart Our Business Startups Act (JOBS Act),¹ Congress *may* have swept away decades of painfully crafted law and lore focused on the “manner-of-offering” element of the private placement exemption codified in former Section 4(2) of the Securities Act of 1933 (Securities Act).² My use of the word “may” is deliberate, given that Congress considered, but ultimately rejected the more direct approach—which had been taken in a precursor bill³—of amending the statutory exemption itself to eliminate the regulatory prohibitions against general solicitation and general advertising that the Securities and Exchange Commission (Commission) and some courts have read into the somewhat cryptic language of the statute: “The [registration] provisions of Section 5 [of the Securities Act] shall not apply to … transactions by an issuer not involving any **public offering**” (emphasis added). Other

than re-numbering former Section 4(2) as Section 4(a)(2), Congress stepped back from the brink and chose not to modify the language of the statutory exemption.

Instead, the JOBS Act drafters directed the Commission, through Title II, to act within 90 days of the statute’s enactment (on or about July 4, 2012) to amend the exemptive safe harbors set forth in Rule 506 of Regulation D (exempt private offerings by issuers) and Rule 144A (exempt private resales to Qualified Institutional Buyers, or QIBs), to lift the express (in the case of Regulation D) and implied (in the case of Rule 144A) prohibitions against general solicitation and general advertising contained in these rules. There is a significant “catch”—all purchasers in an amended Rule 506 offering must be “accredited investors,” and the Commission must specify the “methods” whereby issuers will be deemed to have taken “reasonable steps to verify” the eligibility of each purchaser. In marked contrast, no such “verification” requirement will apply to a resale transaction covered by amended Rule 144A—a seller need only have a reasonable belief that all purchasers are QIBs.

According to staff members of the SEC’s Division of Corporation Finance, which is responsible for drafting proposed rule amendments, the Commission and its staff are aware of the difficult interpretive issues raised by the Congressional decision to change the law thru agency rulemaking rather than statutory amendment. Among these issues are: (1) the impact, if any, on existing jurisprudence governing private placements conducted outside the ambit of the Commission’s exemptive safe harbors, under Securities Act Section 4(a)(2) and the widely recognized (if uncodified) private resale exemption, so-called Section 4 “(1-½)”; and (2) the implications for exempt private offerings of other provisions of the JOBS Act intended

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to facilitate capital formation, such as the new “testing-the-waters” exemption for Emerging Growth Companies (EGCs).⁴ In particular, significant questions have emerged regarding the applicability of the Securities Act integration doctrine.

Title II of the JOBS Act: The Basics

Like the remainder of the JOBS Act, Title II is aimed primarily at expanding the menu of cost-effective capital-raising options for EGCs, whether prior to or after such companies’ IPOs.⁵ Once the Commission amends Rules 506 and 144A, however, companies of any size or Commission reporting status will benefit from the elimination of existing “manner-of-offering” constraints on the conduct of private offerings.⁶

Section 201(a) of the JOBS Act requires the Commission to accomplish two key rulemaking objectives on or before early July 2012:

1. Amend Rule 506 “to provide that the prohibition against general solicitation or advertising contained in ... [Rule] 502(c) [of Regulation D] ... shall not apply to offers and sales of securities made pursuant to ... [Rule] 506, provided that all purchasers of the securities are accredited investors.” Issuers relying on the amended safe harbor must “take reasonable steps to verify that purchasers of the securities are accredited investors, using such methods as determined by the Commission.”

2. Amend Rule 144A(d)(1) “to provide that securities sold under such revised exemption may be offered to persons other than qualified institutional buyers, including by means of general solicitation or general advertising, provided that securities are sold only to persons that the seller and any person acting on behalf of the seller reasonably believe is a qualified institutional buyer.”

Congress emphasized that use of general solicitation and/or advertising techniques to

communicate with a larger pool of potential investors under amended Rule 506 would not alter the “private” character of an otherwise exempt offering. Specifically, Section 201(a)(1) of the JOBS Act states that Rule 506, as thus revised, “shall continue to be treated as a regulation issued under section 4(2) [now 4(a)(2)] of the Securities Act” New Section 4(b) of the Securities Act in turn makes clear that “[o]ffers and sales exempt under ... [amended Rule] 506 ... shall not be deemed public offerings under the Federal securities laws as a result of general advertising or general solicitation.” No such “savings clauses” protect sellers that use general solicitation and/or general advertising in connection with Rule 144A

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transactions. Nor did Congress do anything to level the playing field between Rule 506 offerings, which are exempt from state “blue-sky” laws, and Rule 144A offerings, which continue to require compliance with such laws (absent the availability of a state-created exemption).

Open Questions

Until the Commission issues a proposing release, it is difficult to predict how the many questions raised by Title II will be answered. What follows is a non-exhaustive summary of issues that are now the focus of lively debate among the various constituencies potentially affected by the JOBS Act, some of which are outlined in pre-rulemaking comment letters.⁷

“Reasonable Steps to Verify” Accredited Investor Status

Section 201(a)(1) of the JOBS Act expressly states that all purchasers in an amended Rule 506 offering must be “accredited investors”: “[T]he prohibition against general solicitation or general advertising contained in section 230.502(c) ... shall not apply to offers and sales of securities made pursuant to section 230.506; *provided that all purchasers of the securities are accredited investors*” (emphasis added). Yet the statute goes on to instruct the Commission to enumerate, by rule, “*reasonable steps to verify that purchasers ... are accredited investors*, using such methods as determined by the Commission.” The statute is silent with respect to the consequences of a sale to a non-accredited investor, even if an issuer complies with all Commission-prescribed verification methods.

The Commission’s most difficult rulemaking challenge will be to find the right balance between loosening the “manner-of-offering” restrictions and minimizing the risks of both fraud and disqualifying sales. To this end, the Commission and its staff likely will look in the first instance to the plain language of the statute and, next,

to the relatively sparse legislative history. Also at the Commission’s disposal, of course, is the broad exemptive power conferred by Section 28 of the Securities Act, which the Commission presumably would wield (if at all) only to the extent consistent with Congressional intent. Generally speaking, this intent is to reduce the burdens on “smaller”-business capital formation with the ultimate goal of stimulating U.S. job growth.⁸

Some commentators have urged the Commission, in amending Rule 506, to inject into this rule the “reasonable belief” standard that currently governs an issuer’s determination of whether a potential buyer qualifies as an “accredited investor” within the meaning of Rule 501(a) of Regulation D. Other provisions of Regulation D unaffected by the JOBS Act also employ the concept of “reasonableness” in measuring the adequacy of an issuer’s diligence.⁹ Notably, the Rule 501(a) definition of “accredited investor”—which Congress did not purport to change via the JOBS Act—is framed in the disjunctive, to encompass either (1) a person who, at the time of sale, actually fits within any of eight prescribed categories of individuals or entities deemed able to fend for themselves in a private placement;¹⁰ or (2) a person whom the issuer *reasonably believes* fits within any of these categories at the time of sale. As one commentator aptly observed, this general “approach reflects a practical judgment [by prior Commissions] that the usefulness of Rule 506 would be substantially undermined if the exemption would be lost based on second-guessing of reasonable but erroneous determinations by offering participants.”¹¹

What indicia of Congressional intent can we glean from the legislative record? There is evidence of bipartisan support for the proposition that some curbs on open-ended solicitations via the use of unrestricted electronic communications media will be needed, to reduce the risk that non-accredited investors will misrepresent their “accredited” status. The House sponsor of the amendment to a predecessor bill adding what became Section 201(a)(1)’s “reasonable steps to

verify” requirement, Democratic Representative Maxine Waters of California, expressed this view:

This amendment would clarify that the SEC shall write rules to require that the issuer of a security, using the exemption provided for under this bill shall take reasonable steps to verify their purchase[r]s are accredited investors using such methods as determined by the commission.

Mr. Chairman [of the House Financial Services Subcommittee on Capital Markets and Government Sponsored Enterprises, Scott Garrett], I understand that lifting the ban on general solicitation and general advertising on private offerings may make sense that those offerings are only sold to accredited investors. We know that because of their wealth or their level of sophistication, accredited investors are not in need of as many protections as the average retail investor.

And we know that with the current prohibition on [general] solicitation and advertising it can be tough for a company to connect with accredited investors who may be interested in investing in their company.

But I am concerned about the process in which accredited investors verify that they are in fact accredited. As I understand it, it is currently a self-certification process. This obviously leaves room for fraud.

In testimony from the North American Securities Administration Association the state securities commissioner from Arkansas notes it is going to be impossible to limit the sale to only accredited investors when issuers advertise to everyone. Indeed, there will be no reason to believe that any investor seduced by public advertising will hesitate to be dishonest with completing the investor suitability questionnaire.

That is why I have offered this amendment. My amendment would require the SEC when issuing a rule to provide for the exemption under Representative McCarthy’s bill [H.R. 2940, Title II’s predecessor] to include a provision mandating that issuers take reasonable steps to verify investor status as an accredited investor.

If we are rolling back protections for our targeted audience of sophisticated individuals, we must take steps to ensure that those folks are in fact sophisticated.

This, to me, seems like a common sense amendment. And I hope I can receive bipartisan support.^[12]

This amendment was incorporated without objection into the bill that eventually became Title II.

Based on the foregoing, it appears that the Congressional architects of Title II were concerned that potential investors would attempt to deceive issuers and other offering participants regarding their qualifications as “accredited investors” if the floodgates of general solicitation and general advertising were opened. That concern would not be undermined if the Commission construed the phrase “reasonable steps to verify” to mean that issuers (and persons acting on their behalf) must adopt diligence mechanisms sufficient under all relevant facts and circumstances to formulate a “reasonable belief” that all purchasers in a “private offering” effected pursuant to general solicitation/advertising are “accredited.” This construction would not require affirmative proof that all purchasers in a given private offering are in fact “accredited,” but rather that the issuer (and/or placement agent or other offering participant) has undertaken the level of diligence that is “due” in connection with a particular offering, taking into account such pertinent factors as the availability of current financial and other information relating to a potential investor’s sophistication

and/or accumulated wealth. For example, is the investor a registered investment company reporting to the Commission, an insurance company that regularly provides statutory financial statements to state insurance regulators that can be furnished to the issuer or its agent, a public pension fund that regularly reports information on its financial position and makes this information available to the issuer or its agent? One can hope that the Commission would look for models to other “principles-based” safe harbors that enumerate a non-exclusive set of factors for issuers to weigh in determining how best to comply with the stated “principle”—the fundamental objective of the safe harbor itself.¹³

This evidence may be somewhat easier to collect from institutions subject to regulatory disclosure obligations than from individual investors who have legitimate expectations of financial privacy. Borrowing a concept from the Commission’s shareholder proposal rule,¹⁴ the Commission might consider, as a potentially reliable indicator of an individual’s accredited investor status, a written representation from that person’s broker-dealer or investment adviser stating that its customer falls within one or more of these eligible categories and outlining the specific grounds for such representation.¹⁵ Because these traditional “gatekeepers” owe suitability or fiduciary obligations to their customers and are subject to comprehensive Commission regulation by virtue of their registration as, respectively, they have ample incentive to make accurate, diligence-based representations regarding their customers’ eligibility.

This suggestion is not intended to import into amended Rule 506, once it becomes unnecessary, the concept of a “pre-existing, substantive relationship” between a registered broker-dealer acting as placement agent and customer-offerees that can serve to rebut a presumption that such offerees were attracted by general solicitation or general advertising. What I am suggesting is that the Commission’s longstanding recognition

of the appropriateness of an issuer’s reliance on a statutory “gatekeeper’s” performance of duties owed to customers in specific situations—duties that arise independently and are enforceable under the federal securities laws—might prove to be as useful in this context as it has proven to be elsewhere.

Nothing in the JOBS Act would diminish a registered broker-dealer’s suitability obligations to customers when recommending investment in a private placement, as FINRA explained in a May 2012 interpretive release pertaining to suitability requirements under FINRA Rule 2111:

Question 5: ...Does the elimination of the general solicitation prohibition mean that broker-dealers no longer have suitability obligations regarding private placements?

Answer 5: No. The JOBS Act removes certain marketing impediments, but not a broker-dealer’s suitability obligations. [A] broker-dealer’s general solicitation of a private placement through the use or distribution of marketing or offering materials ordinarily would not, by itself, constitute a recommendation triggering the application of the suitability rule [FINRA Rule 2111]. When a broker-dealer “recommends” a private placement [to its customer], however, the suitability rule applies.^[16]

The Commission’s decision as to how (and to what extent) to marry the “reasonable belief” standard reflected in Rule 501(a)’s definition of “accredited investor” to the proposed amendments to Rule 506 related to general solicitation may be critical to issuers evaluating whether to assume the heightened risk of a disqualifying sale along with what are likely to be increased diligence costs. It might be helpful in this regard if the Commission added regulatory language providing that an unintentional or inadvertent sale of securities to a non-accredited investor would not prevent an issuer’s reliance upon the exemptive safe harbor for the entire offering if the issuer

could demonstrate a “reasonable belief” as to the investor’s eligibility under Rule 501. This belief could be established by showing that an issuer adhered to the verification methods specified by Commission rule.

“Quiet” Private Offerings Under “Old” Rule 506

According to the SEC staff report on Regulation D published earlier this year, most issuers raising capital under current Rule 506 in the past few years have sold securities almost exclusively to accredited investors.¹⁷ Some issuers contemplating a private placement in the future thus may have no need to resort to the Internet or other forms of unrestricted media communication to locate investors, whether accredited or otherwise. Depending on the Commission’s proposed definition of the phrase “reasonable steps to verify” the accredited investor status of purchasers, at least some issuers may determine that the costs associated with the enhanced diligence likely to be required to establish purchaser eligibility may outweigh any countervailing benefits that might be derived from widening the pool of potential purchasers.

There is some hope for those who may prefer to have the option of pursuing a “traditional” or “quiet” Rule 506 offering unaccompanied by general solicitation or general advertising. At a recent Practising Law Institute (PLI) conference on the JOBS Act, Meredith B. Cross, Director of the Commission’s Division of Corporation Finance, reportedly stated that, “in her view, the new verification requirement would apply only to Rule 506 offerings that are generally solicited or advertised, and not to traditional private placements in that sphere.”¹⁸ Accordingly, issuers still might have a choice of offering and selling securities to up to 35 non-accredited investors and an unlimited number of accredited investors under “old” Rule 506, so long as the general solicitation/general advertising prohibitions are observed. As Ms. Cross cautioned, however,

the Commission ultimately could decide (though not mandated by the JOBS Act) to extend the new “reasonable steps to verify” standard to such “quiet” 506 offerings. For that matter, the Commission could foreclose the choice of a “quiet” Rule 506 offering entirely—we will simply have to wait and see.

Ms. Cross further indicated that the Commission would not re-visit the “accredited investor” definition in Rule 501(a) until at least 2014, because Section 413(b)(2) of the Dodd-Frank Act by its terms does not permit earlier adjustment of the definition with respect to individual investors.¹⁹ This is likely in response to some commentators who had recommended that the Commission raise the “accredited investor” threshold for individuals now, rather than wait.²⁰

The Statutory Private Placement Exemption in Section 4(a)(2)

Because Congress did not amend the substance of the statutory private placement exemption now codified in Section 4(a)(2) of the Securities Act, practitioners will continue to grapple with difficult publicity issues on a case-by-case basis in the context of “traditional” private placements conducted outside the regulatory safe harbors. For the first time, however, the Securities Act states unequivocally that general solicitation and/or general advertising can be used to offer and sell securities without impairing the “private” nature of an unregistered offering—but only if all purchasers qualify as “accredited investors.” Does this mean that companies will never be able to rely on Section 4(a)(2) in situations where the expanded safe harbor technically might not be available because of a single sale to a non-accredited investor? Or will the de-regulation of offering activity lead to a change in how the courts and the Commission analyze the parameters of the statutory exemption for private offerings? Perhaps all we can safely predict at this point is that the Commission is likely to adhere to its customary

practice of leaving such vexing questions to the courts.

The Integration Doctrine in a Post-JOBS Act World

Even before the Commission publishes its proposing release, questions are being raised regarding the application of the “integration” doctrine when offerings involving general solicitation or general advertising become permissible under amended Rules 506 and 144A. Whether or not the Commission will have an opportunity to address any of these questions in the initial wave of mandatory rulemaking is unclear, but an early dialogue among practitioners on possible answers may be helpful to Commission rule-writers.

Over the years, the integration doctrine has evolved beyond its original objective—to prevent evasion of Securities Act Section 5’s registration requirements, “by separat[ing] parts of a series of related transactions, the sum total of which is really one [non-exempt] offering, and claim[ing] that a particular part is a nonpublic [exempt] transaction....”²¹ The Commission fashioned a five-factor test in 1962, later mirrored in Regulation D and other regulatory safe harbors, to guide the determination whether multiple unregistered offerings were part of a single transaction that in the aggregate might not be protected by a regulatory safe harbor.²² By the mid-to-late 1980s, the Commission’s staff was applying integration concepts to concurrent private and registered offerings to analyze whether the two should be combined, with the publicity attendant to the public offering almost inevitably precluding the issuer’s reliance on an exemption for the private offering. Seeking a practical solution to an obvious problem, the staff through the no-action letter process eventually re-focused the analysis of such concurrent offerings on the following: (1) whether the offers and sales in the private transaction were made only to QIBs and a few institutional accredited investors (IAIs); and (2) whether issuer’s counsel could represent that a

valid private placement exemption was available for that transaction.²³

The Commission greatly simplified the integration doctrine as applied to simultaneous registered and private exempt offerings in 2007. It clarified that the mere filing of a Securities Act registration statement “does not, *per se*, eliminate a company’s ability to conduct a concurrent private offering, whether it is commenced before or after the filing of the registration statement.”²⁴ Issuers would not be confined any longer to soliciting a particular type and number of financially sophisticated investors when seeking private capital, either before or during the pendency of a registered offering.²⁵ In other words, the appropriate focal point for Securities Act analysis of these side-by-side offerings henceforth would be on “how the investors in the private offering are solicited—whether by the registration statement or through some other means that would not otherwise foreclose the availability of the Section 4(2) exemption.”²⁶

With the integration doctrine thus restored to its original dimensions, the evaluation of multiple unregistered offerings for Securities Act compliance, how should that doctrine be applied in the wake of the JOBS Act? Perhaps the most interesting of the questions posed thus far center on the ramifications for the integration doctrine of Title II’s de-regulation of offers and new Section 5(d)’s “testing-the-waters” exemption for EGCs. Any issuer soon will be able to use general solicitation/advertising to find potential investors without risking the loss of the exemptive safe harbor provided by amended Rule 506 if sales are made only to accredited investors, while EGCs can engage in communications with certain institutional investors that otherwise would be considered illegal “gun-jumping.” But can an issuer thread the needle successfully in a variety of dual-track offering scenarios, simultaneously using both Section 5(d) and amended Rule 506 (or the old “quiet” Rule 506, if still available) to gauge potential investors’ appetite for restricted

vs. unrestricted IPO securities for cash or, alternatively, pursue in tandem a privately negotiated M&A transaction or an IPO? Or must an EGC proceed with an IPO once it begins communicating with QIBs and IAIs in reliance upon Section 5(d)?²⁷ One commentator has suggested that the Commission preserve maximum flexibility for issuers in such situations, by making it “clear that testing-the-waters by an emerging growth company under … [Section] 5(d) of the Securities Act, whether before or during the pendency of a registration statement, will not prevent a company from engaging in an exempt offering so long as the requirements for testing-the-waters are met and the requirements for the exempt offering are otherwise met.”²⁸

Several commentators have recommended that the Commission re-affirm its interpretive statement relating to application of the integration doctrine in a cross-border context, published when it adopted Regulation S in 1990. It had announced that “[l]egitimate selling activities carried out in the United States in connection with an offering of securities registered under the Securities Act or exempt from registration pursuant to the provisions of section 3 or 4 of the Securities Act will not constitute directed selling efforts with respect to offers and sales made under Regulation S.”²⁹ This non-integration position arose from concerns that any offering activity in the United States, which in 1990 could not have involved general solicitation or general advertising, would be inconsistent with Regulation S’s ban on U.S. directed selling efforts. The question now is whether the Commission’s non-integration position remains intact with respect to contemporaneous Regulation S and U.S.-directed offerings that soon may be accompanied by general solicitation or general advertising under amended Rule 506 and/or amended Rule 144A. Those commentators that have expressed a view on this subject thus far have said yes, given that a registered U.S. offering now may occur at the same time as a valid Regulation S offering outside the United States.³⁰

Questions also have been raised as to the ability of issuers to raise private capital under Section 4(a)(2) or “quiet” Rule 506 within six months before or after an offering accompanied by permissible general solicitation or general advertising under amended Rule 506.³¹ In this connection, it has been suggested that the Commission revive its 2007 proposal to reduce the six-month safe harbor to 90 days, or even to 30 days.³² Finally, while issuers will be free to make concurrent registered and exempt “public” offerings under amended Rule 506 (and/or in an underwritten Rule 144A transaction) without regard to the need for compliance with the 2007 Commission interpretive position discussed above, some specific guidance would be welcome; for example, may the same QIBS and IAIs invest in both of these offerings?

Conclusion

There is every reason to believe that the Commission’s proposed rules under Title II will reflect the same flexibility and pragmatism that have characterized the Division of Corporation Finance JOBS Act interpretations issued to date.

Given the extremely short implementation deadline, the Commission’s staff has signaled that some of the open questions discussed above are unlikely to be resolved during the initial round of mandatory JOBS Act rulemaking. Final resolution of the most difficult of these questions, such as the implications for the Section 4(a)(2) private placement exemption of Congress’s surgical elimination of the regulatory ban on general solicitation and general advertising as a condition to reliance on the Rule 506 and Rule 144A safe harbors, ultimately may be for the courts.

Notes

1. Pub. L. No. 112-106, 126 Stat. 306 (2012).
2. For excellent analyses of such law and lore, see Stanley Keller, “A Retrospective on Changes in Regulation of Securities Offerings,” 26 INSIGHTS 4 (April 2012), and an American Bar Association report

primarily authored by William J. Williams, Jr., entitled “Law of Private Placements (Non-Public Offerings) Not Entitled to Benefits of Safe Harbors—A Report by the Committee on Federal Regulation of Securities, ABA Section of Business Law” (Nov. 2010), published in 66 Bus. Law 85 (2010) (Law of Private Placements).

3. H.R. 2940, Access to Capital for Job Creators Act. According to the report of the House Committee on Financial Services upon submitting H.R. 2940 to the full House of Representatives in late October 2011, former Section 4(2) of the Securities Act would have been amended by adding at the end, language to the effect that offerings conducted in reliance upon the statutory exemption would be deemed non-public “whether or not such transactions involve general solicitation or general advertising.” H.R. Rep. No. 112-263, 112th Cong., 1st Sess. 1 (Oct. 31, 2011). Had this particular version of the bill become law, Section 4 would have read: “The provisions of Section 5 shall not apply to -- ... (2) transactions by an issuer not involving any public offering, *whether or not such transactions involve general solicitation or general advertising.*” *Id.* at 6 (emphasis in the original). The House passed H.R. 2940 in early November 2011. *See* 157 Cong. Rec. H7314 (daily ed. Nov. 3, 2011). In early March 2012, the italicized language was stripped out of H.R. 2940, and certain other language added, to create the provisions that were to become Title II of H.R. 3606. *See* 158 Cong. Rec. H1260–H1264 (daily ed. March 7, 2012). A new Section 4(b) of H.R. 2940, the substance of which appears in Section 201(a)(1) of the JOBS Act, directed the Commission to eliminate the ban on general solicitation and general advertising applicable to Rule 506 offerings. According to the sponsor of H.R. 2940, Republican Representative Kevin McCarthy of California, “this amendment is designed to make several small changes to make sure the regulation D, rule 506 provision in this bill meets its original intent. In consultation with the Securities and Exchange Commission and our friends on the other side of the aisle, we identified several areas where the language in the bill could have had some unintended consequences that may have limited the effectiveness of the provision or expanded its reach beyond what we originally intended. * * * This amendment does three things: [1] Clarifies that [the general solicitation and] general advertising provision should only apply to Regulation D, rule 506 of the securities [act] offerings; [2] Protects investors by allowing for [general solicitation and] general advertising in the secondary sale of these securities, so long as only qualified institutional buyers purchase the securities; [and 3] Provides consistency in the interpretation for regulators that general advertising should not cause these private offerings to be considered public offerings.” *Id.* at H1260-1261.

4. Section 101 of the JOBS Act defines the term “emerging growth company,” for purposes of both the Securities Act and the Securities Exchange Act of 1934, as amended, to mean an issuer that had total annual gross revenues of less than \$1 billion “during its most recently

completed fiscal year” (an amount that must be indexed to inflation by the Commission every five years); provided that the first sale of common equity securities of the issuer pursuant to an effective registration statement did not occur on or before December 11, 2011. An EGC may retain this favored status for up to five years.

5. An IPO for purposes of Title I of the JOBS Act is an issuer’s first sale of common equity securities under an effective Securities Act registration statement, which “could include offering common equity pursuant to an employee benefit plan on a Form S-8 as well as a selling shareholder’s secondary offering on a resale registration statement [on Form S-3 or F-3].” Question 2 of Title I FAQs. *See also* note 4, above.

6. A recently published report by staff of the Commission’s Division of Risk, Strategy and Financial Innovation indicates that public and private issuers alike tapped the private markets in reliance upon one of the three Regulation D exemptive safe harbors (Rules 504, 505, and 506), with 91.6% of all such offerings during the period studied (2009 through the first quarter of 2011) conducted under Rule 506. *See* Vlad Ivanov and Scott Baugess, “Capital Raising in the U.S.: The Significance of Unregistered Offerings Using the Regulation D Exemption (February 2012) (“Reg. D Report”), available at http://www.sec.gov/info/smallbus/acsec/acsec102111_analysis-reg-d-offering.pdf.

7. Following precedent established with passage of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, the Commission is taking comments on the JOBS Act as a prelude to the institution of formal rulemaking processes. *See* the Commission webpage entitled “Public Comments on SEC Regulatory Initiatives Under the JOBS Act,” at <http://www.sec.gov/spotlight/jobsactcomments.shtml>.

8. The preamble to the JOBS Act defines its fundamental purpose as follows: “To increase American job creation and economic growth by improving access to the public capital markets for emerging growth companies.”

9. *See, e.g.*, Rule 502(d) (“The issuer shall exercise **reasonable care** to assure that the purchasers ... are not underwriters within the meaning of section 2(a)(11) of the [Securities] [A]ct) (emphasis added); Rule 501(a)(A) “purchaser representative” means either a person who satisfies several conditions enumerated in the rule, or “who the issuer **reasonably believes** satisfies all of ... [such] conditions.”).

10. *See* Rule 501(a)(1)-(8).

11. Comment Letter from Robert E. Buckholz, Chair, Committee on Securities Regulation of the New York City Bar Association, to Elizabeth M. Murphy, Secretary, Securities and Exchange Commission, dated May 20, 2012 (“NYCBA Letter”), at 2-3, available at <http://www.sec.gov/comments/jobs-title-ii/jobstitleii-8.pdf>.

12. House Financial Services Subcommittee on Capital Markets and Government Sponsored Enterprises Holds Markup on HR 1965, HR 2167, HR 2930, HR 2940 and a Draft Bill Concerning Small Companies

and Regulatory Relief, 112th Cong., 1st Sess. (Congressional Hearing held Oct. 5, 2011), Congressional Quarterly Transcripts at 8-9 (note that the official transcript of this hearing has not been published in the Congressional Record). The Republican Chair of the House Financial Services Subcommittee, Rep. Scott Garrett of New Jersey, said “I believe that it is a good amendment. I also encourage support of the amendment.” *Id.* at 9. Representative Maxine Waters, whose statement is quoted above in the text, indicated that she had consulted with the SEC in framing her amendment. *Id.* It is worth noting in this regard that the Commission has expressed opposition to self-certification practices in the past, where used by non-broker-dealer operated website platforms for issuer private offerings. *See* SEC Interpretation: Use of Electronic Media, SEC Rel. No. 34-42728 (April 28, 2000) (“2000 E-Media Release”), at notes 85-88 and accompanying text (this release is available at <http://www.sec.gov/rules/interp/34-42728.htm>). The focal point of discussion here was the Commission’s endorsement of the staff’s application of the “pre-existing, substantive relationship” exception to the general solicitation/general advertising prohibition in connection with password-restricted, online private offerings, with the caveat that this exception would be available only where prospective offerees had established such a relationship with a registered broker-dealer before gaining access to a particular private offering. What the Commission did not say in this release, however, was that self-certification was per se inappropriate in situations where a registered broker-dealer operates such a platform and vets the suitability of prospective offerees.

13. Examples of the non-prescriptive, multi-factor analytical approach advocated in the text are codified in Securities Act Rules 502(d) (non-exclusive list of measures issuers can take to establish the requisite “exercise of reasonable care” in assuring that all purchasers are not underwriters within the meaning of Section 2(a)(11) of the Securities Act); 175 (antifraud safe harbor for issuer forward-looking statements made or re-affirmed in “good faith” and with a “reasonable basis”); and 176 (circumstances affecting the determination of what constitutes “reasonable investigation” and “reasonable grounds” for belief under Section 11 of the Securities Act).

14. Exchange Act Rule 14a-8(a)(2), as interpreted by the staff in Staff Legal Bulletin 14F (Oct. 18, 2011) (available at <http://www.sec.gov/interp/legall/cfslb14f.htm>) offers “street-name” holders of voting equity securities subject to the Commission’s proxy rules, who by definition do not have record title to their securities for purposes of applicable state law, the option to substantiate the requisite level and length of beneficial ownership in connection with the submission of a shareholder proposal by providing the company with a written statement from the custodial record holder of those securities—which must be a broker-dealer, bank or other financial intermediary that is a participant in the Depository Trust Company (DTC)—“verifying” the requisite beneficial ownership.

15. Others have made similar suggestions; *see, e.g.*, NYCBA Letter at 2-3; Comment Letter from Annemarie Tierney, General Counsel and Corporate Secretary, SecondMarket Holdings, Inc., to Elizabeth M. Murphy, Secretary, U.S. Securities and Exchange Commission, dated May 25, 2012, at 1, available at <http://www.sec.gov/comments/jobs-title-ii/jobtitleii-16.pdf>
16. FINRA Regulatory Notice 12-25 (posted May 18, 2012; effective July 9, 2012), available at <http://www.finra.org/Industry/Regulation/Notices/2012/P126432>.
17. Reg. D Report at 6 (footnote omitted) (“The average amount of non-accredited investors in the Reg. D offerings [most of which were conducted under Rule 506, as discussed above in note 8] over the entire period is 0.1, while the median is 0. In fact, in approximately 90% of the offerings there are no non-accredited investors.”).
18. Bloomberg BNA Securities Law Daily (May 31, 2012), available by subscription at http://news.bnacom/sdln/display/batch_print_display.adp (reporting on this PLI conference entitled “*JOBS Act 2012: What You Need to Know Now*,” held in New York, New York on May 31, 2012; the webcast version of this day-long conference will be available for replay at www.pli.edu in the near future).
19. Section 413(b) of the Dodd-Frank Act makes clear that subsequent Commission review must occur “not earlier than” four years after enactment (in mid-2010). The Commission effected the initial adjustment prescribed by Section 413(a) last year, when the agency amended the net-worth component of the individual “accredited investor” definition in Rule 501(a) to exclude the value of an individual’s primary residence. *See* Net Worth Standard for Accredited Investors, SEC Rel. No. 33-9287 (Dec. 21, 2011), available at <http://www.sec.gov/rules/final/2011/33-9287.pdf>.
20. *See* Comment Letter from Paul Schott Stevens, President and CEO, Investment Company Institute, to Elizabeth M. Murphy, Secretary, Securities and Exchange Commission, dated May 21, 2012, available at <http://www.sec.gov/comments/jobs-title-ii/jobtitleii-13.pdf>; Comment Letter from Fund Democracy, Consumer Federation of America, Consumer Action, AFL-CIO, Americans for Financial Reform, to Elizabeth M. Murphy, Secretary, U.S. Securities and Exchange Commission, dated May 24, 2011, available at <http://www.sec.gov/comments/jobs-title-ii/jobtitleii-14.pdf>.
23. Nonpublic Offering Exemption, SEC Rel. No. 33-4552 (Nov. 6, 1962), available at <http://www.sec.gov/rules/final/33-4552.htm>. In this release, the Commission posited the now-famous “five-factor test” for determining whether multiple unregistered offerings should be integrated: (a) whether the sales are part of a single plan of financing; (b) whether the sales involve issuance of the same class of securities; (c) whether the sales are made at or about the same time; (d) whether the same type of consideration is received; and (e) whether the sales

are made for the same general purpose. Citing SEC Rel. No. 33-4552, a Note to Rule 502(a) of Regulation D repeats these factors without discussion of how they should be weighed. The Commission thereafter adopted a series of integration safe harbors under the Securities Act that gave issuers some comfort that multiple offerings would not be integrated if issuers satisfied certain conditions. *See, e.g.*, Rules 502(a) and 500(g) of Regulation D (offers/sales made six months before or after completion of a Reg. D offering will not be integrated with such offering; generally, simultaneous Reg. S offerings offshore will not be integrated with “coincident” Reg. D offerings within the United States); Rule 144A(e) (offers/sales of securities under Rule 144A will not affect the availability of any exemption or safe harbor relating to any previous or subsequent offer or sale of such securities by the issuer or any prior or subsequent holder); Rule 701(f)(non-integration of exempt employee benefit plan offers/sales with other registered or exempt offerings); Rule 251(c) of Regulation A (non-integration of Reg. A offers and sales with exempt or registered offers and sales before or after the Reg. A offering). *See also* Offshore Offers and Sales, SEC Rel. No. 33-6863, 55 Fed. Reg. 18306 (May 2, 1990) (“Regulation S Adopting Release”), at Parts III.B.1.b. and C.1.

22. *See* note 21, above.

23. Limited exceptions to integration of concurrent public and private offerings (among other things) were articulated by the Division of Corporation Finance in no-action letters such as Black Box, Inc. (June 26, 1990) and Squadron Ellenoff, Pleasant & Lehrer (Feb. 28, 1992).

24. Revisions of Limited Offering Exemptions in Regulation D, SEC Rel. No. 33-8828 (Aug. 3, 2007) (“2007 Release”), at Part II.C., available at <http://www.sec.gov/rules/proposed/2007/33-8828.pdf>).

25. The Commission explained that “our determination as to whether the filing of a registration statement should be considered to be a general solicitation or general advertising that would affect the availability of the Section 4(2) exemption for such a concurrent registered offering should be based on a consideration of whether the investors in the private placement were solicited by the registration statement or through some other means that would otherwise not foreclose the availability of the Section 4(2) exemption. This analysis should not focus exclusively on the nature of the investors, such as whether they are ... [QIBs] or institutional

accredited investors, or the number of such investors participating in the offering; instead, companies and their counsel should analyze whether the offering is exempt under Section 4(2) on its own, including whether securities were offered and sold to the private placement investors through the means of a general solicitation in the form of a registration statement.” 2007 Release at 55-56.

26. *Id.* (emphasis in the original). The Commission also adopted the staff’s construction of Securities Act Rule 152: “a company’s contemplation of filing a Securities Act registration statement for a public offering at the same time that it is conducting a Section 4(2)-exempt private placement would not cause the Section 4(2) exemption to be unavailable for that private placement.” *Id.* at 54. At the same time, the Commission warned that, “[i]n these circumstances, companies should be careful to avoid any pre-filing communications regarding the contemplated public offering that could render the Section 4(2) exemption unavailable for what would be an otherwise exempt private placement.” *Id.* at 54 note 124.

27. Cf. Securities Act Rule 254(d)(“Where an issuer has a bona fide change of intention and decides to register an offering after using the [Reg. A Rule 254 “test-the-waters”] process permitted by this section without filing the offering statement prescribed by Rule 252, the Regulation A exemption for offers made in reliance upon this section will not be subject to integration with the registered offering, if at least 30 calendar days have elapsed between the last solicitation of interest and the filing of the registration statement with the Commission, and all solicitation of interest documents have been submitted to the Commission.”).

28. Stanley Keller, “*Integration of Private and Public Offerings Update*” (May 30, 2012)(“Keller”), submitted in connection with his participation as a speaker at the PLI conference cited in note 24, above.

29. Regulation S Adopting Release, 55 Fed. Reg. at 18312.

30. *See, e.g.*, Keller at 47-48; NYCBA Letter at 4.

31. Keller at 46-47; Comment Letter from Jeffrey W. Rubin, Chair, Federal Regulation of Securities Committee, American Bar Association, to Elizabeth M. Murphy, Secretary Securities and Exchange Commission, dated April 30, 2012, at 5, available at <http://www.sec.gov/comments/jobtitle-iii/jobtitleii-7.pdf>.

32. *See* Keller at 46.