PUBLICATION

Impact of the JOBS Act on Public Companies (No. 1) [Ober|Kaler]

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A periodic bulletin keeping small businesses informed about current developments in securities law and related matters.

President Obama signed the Jumpstart Our Business Startups Act (Act) into law on April 5, 2012. This Bulletin discusses the new law's impact on public companies (i.e. those companies that have publicly sold stock or are otherwise required to file reports with the Securities and Exchange Commission (SEC)) and those that are considering going public. For a discussion of the provisions of the Act impacting private (non-SEC reporting) companies, please see our April 2012 Bulletin, "Impact of the JOBS Act on Private Companies."

Scaled Disclosure Requirements and Other Changes for "Emerging Growth Companies"

The Act creates a new category of issuer called an "emerging growth company" (EGC). An EGC is a company with less than $1 billion in gross annual revenues, measured as of the end of its most recent fiscal year, that first sold common stock pursuant to an effective registration statement after December 8, 2011. An EGC retains its status as such for five years unless during that period its gross annual revenues exceed $1 billion, it offers more than $1 billion in non-convertible debt, or its "public float" (i.e. the market value of its common equity held by non-affiliates) equals at least $700 million. In their Securities Act of 1933 registration statements to publicly sell stock, EGCs may take advantage of certain scaled disclosure requirements otherwise applicable to smaller reporting companies – those with a public float of less than $75 million. These include providing two years of audited financial statements and discussion of only two years of financial results in the company's management's discussion and analysis of financial condition and results of operations, as well as the scaled executive compensation disclosure requirements applicable to smaller reporting companies under Item 402 of Regulation S-K. EGCs that are not smaller reporting companies, and therefore required to provide selected financial data, will not be required to provide such data for any years prior to fiscal years that were audited in connection with their initial public offering. The Act also exempts EGCs from new accounting standards until such standards become applicable to private companies (to the extent such standards will apply to private companies). With respect to their Exchange Act reports once their registration statement becomes effective, EGCs may take advantage of the scaled executive compensation disclosure requirements applicable to smaller reporting companies and, like smaller reporting companies, will be exempt from the auditor attestation of internal control over financial reporting requirement pursuant to the Sarbanes-Oxley Act of 2002. Finally, EGCs will be exempt from the say-on-pay and say-on-golden parachute stockholder votes and related disclosure implemented pursuant to the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (Dodd-Frank) (See our January 2011 Bulletin) and the SEC's forthcoming executive compensation rules on pay for performance and pay ratio disclosures required pursuant to Dodd-Frank (See our June 29, 2010 Bulletin), as well as any rules the Public Company Accounting Oversight Board (PCAOB) might implement with respect to audit firm rotation or additional information about the audit or financial statements of the company (such as an auditor discussion and analysis), except to the extent the SEC determines is otherwise necessary.

In addition, EGCs may have the SEC review draft registration statements on a confidential, nonpublic basis as long as the initial filing and all amendments thereto are publicly filed at least 21 days before any road show. EGCs may also "test the waters" by communicating (or having their agent communicate) with qualified institutional buyers and institutional accredited investors to determine whether such entities may have an interest in a contemplated securities offering either before or after the filing of the registration statement with respect to such offering. The Act also permits research reports by a broker or dealer about an EGC that is the subject of a proposed public offering of common equity securities.

Changes Applicable to Private Placement Offerings

Rule 506 Private Placements

As our readers know, any offer or sale of securities must be registered or exempt from registration under both the Securities Act and any applicable state securities laws. The most often-used exemption is Rule 506 under the Securities Act, which exempts from registration (under federal and state law) offers and sales of securities made solely to "accredited investors" and up to 35 non-accredited but "sophisticated" investors. Accredited investors generally include natural persons with income of $200,000 or $300,000 with their spouse or a net worth (excluding their primary residence) exceeding $1 million, and certain institutions, while a "sophisticated" investor means an "investor either alone or with his purchaser representative(s) has such knowledge and experience in financial and business matters that he is capable of evaluating the merits and risks of the prospective investment." The Act loosens the restrictions on general advertising and general solicitation with respect to Rule 506 offerings by providing that such restrictions will not apply to any such offering where all of the purchasers are accredited investors. The SEC must amend its rules in this regard within 90 days of passage of the Act. Such amended rules must require a company relying on this exemption to take "reasonable steps" to verify that the purchasers are accredited investors; this may require companies to go beyond the current standard of solely requiring purchasers to self-certify that they qualify as accredited investors. The Act requires the SEC to similarly amend its rules with respect to the exemption for private resales to qualified institutional buyers pursuant to Rule 144A under the Securities Act.

"Regulation A+" Offerings

The Act authorizes the SEC to create a new exemption from registration for offers and sales of up to $50 million (subject to increase for inflation) of equity securities, debt securities and convertible debt securities within any 12-month period. Such securities may be offered and sold publicly and will be freely re-salable Like current Regulation A, which exempts offerings of up to $5 million in any 12-month period, companies will be required to prepare, file with the SEC and distribute to potential investors an offering statement and will be permitted to "test the waters" to solicit interest in the offering prior to filing. Unlike current Regulation A, the new exemption will not be limited to non-SEC reporting companies, although such companies that take advantage of the new exemption will be subject to some periodic disclosure reporting requirement to be set forth in the SEC rule adopting the exemption. Companies that take advantage of the exemption and sell the securities on a national securities exchange or solely to qualified purchasers, as defined by SEC rule, will be exempt from state registration/exemption requirements. Otherwise, companies will have to register the offering in the states in which they plan to offer and sell the securities, unless another exemption is available under applicable state(s) law.

Although details will be provided by the SEC pursuant to a rulemaking, once implemented, this new offering exemption should be very helpful to small- and mid-size banks and holding companies who are struggling to raise capital but do not want to go through the full-blown SEC registration process.

Threshold for Deregistration

Prior to the Act, companies with total assets exceeding $10 million and a class of securities held by 500 or more holders of record are required to register such class of securities under the Exchange Act, even if they have not publicly sold securities. Companies that are so required to register their securities, or that have publicly offered and sold securities pursuant to a registration statement under the Securities Act, are required to comply with the periodic reporting requirements of the Exchange Act. This means they are required to file annual reports, quarterly reports, proxy statements and current reports with the SEC, among other things. Currently, such companies can only terminate such registration and suspend their periodic reporting obligations if the number of holders of record of such security falls below 300. The Act changes the deregistration threshold for banks and bank holding companies only to 1,200 holders of record; although the Act directs the SEC to issue regulations to implement this change, it revised the Exchange Act itself to increase this threshold. Therefore, banks and bank holding companies that are eligible to deregister and suspend their reporting obligations under the Exchange Act as revised may be able to do so immediately.