



THE JOBS ACT

The bi-partisan Jumpstart Our Business Startups Act (the “JOBS Act”) was passed by Congress on March 27, 2012 and signed into law on April 5, 2012 by President Obama. A hyperlink to the JOBS Act is [here](#). The purpose of the JOBS Act is to increase domestic job growth by improving access to the capital markets for companies, including pre-IPO companies.

The JOBS Act contains significant changes to the existing regulatory scheme regarding capital formation, and it is the first federal law since the financial crisis of 2008 to reduce regulatory burdens on capital formation and on public and private companies. Although some provisions of the JOBS Act are effective immediately, others will require SEC rulemaking over the next 270 days, in addition to the required rulemaking already pending at the SEC under the Dodd-Frank Act. The JOBS Act gives start-ups and other private companies additional flexibility in raising capital, greases the pathway to an IPO for companies that qualify as emerging growth companies (less than \$1 billion in annual revenue) (“EGCs”), and eases certain regulatory burdens on EGCs for a window of up to five years following an IPO.

The JOBS Act (i) permits general solicitations and general advertisements in Regulation D Rule 506 private offerings if securities are sold only to “accredited investors” (e.g., individuals that have a net worth of \$1 million or more or have a certain annual income), (ii) relaxes certain governance, accounting and disclosure requirements for EGCs, (iii) permits

regulated “crowdfunding” (e.g., raising limited amounts of capital over the internet), (iv) increases the size of Regulation A offerings from \$5 million to \$50 million in any 12-month period, and (v) changes the trigger for required Exchange Act registration (i.e., increases the shareholder threshold from 500 to 2,000).

EMERGING GROWTH COMPANIES

The JOBS Act addresses the IPO process and seeks to reduce regulatory burdens for EGCs in order to encourage more public offerings. For EGCs, certain accounting, disclosure and governance requirements are relaxed or postponed for up to five years after an IPO. The JOBS Act:

- allows EGCs to submit draft registration statements to the SEC for confidential review;
- allows EGCs to “test the waters” before a registered offering by allowing EGCs to engage in oral and written discussions with potential investors that are qualified institutional buyers or institutional accredited investors;
- allows EGCs to provide two years (instead of three years) of audited financials in their IPO registration statements;
- delays compliance with certain required disclosures of EGCs relating to Section 404 of the Sarbanes-Oxley Act (internal control over financial reporting auditor’s attestation), say-on-pay, and (the yet to be finalized) disclosures required by the Dodd-

Frank Act on CEO/median compensation pay ratios, and executive compensation and company performance; and

- reduces regulatory restrictions on analysts relating to the publication of research reports on EGCs in the IPO process.

RULE 506 OFFERINGS: GENERAL SOLICITATION AND GENERAL ADVERTISEMENT

The JOBS Act eliminates the prohibition on general solicitation and general advertisement of private placements under Rule 506 of Regulation D, as long as the ultimate purchasers of the offered securities are accredited investors. Rule 506 is a “safe harbor” for the private offering exemption of Section 4(2) of the Securities Act. Subject to compliance with the rule’s conditions, companies using Rule 506 can raise an unlimited amount of money in private offerings. In a Rule 506 offering a company may sell its securities to an unlimited number of accredited investors and up to 35 other purchasers.

The JOBS Act amends Rule 506 by permitting the use of a general solicitation or general advertising (which were previously prohibited), so long as the ultimate purchasers of the offered securities are accredited investors. Issuers will now be able to solicit anyone and may now advertise in any way they see fit, provided that the ultimate investors are accredited investors. In connection with the removal of the general solicitation prohibition, the JOBS Act requires that prior to selling a security to an investor, the company must “take reasonable steps to verify that purchasers of the securities are accredited investors.” The JOBS Act does not set forth the steps that will need to be taken to satisfy this “verification” mandate. Instead, the

SEC is charged with creating the rules that will define which particular methods must be followed¹. Thus, it will be important for a company to follow the SEC’s rulemaking regarding this verification mandate so that it can take advantage of this opportunity to completely change the way it solicits new investors.

In addition, the JOBS Act exempts from broker-dealer registration persons who facilitate Rule 506 offerings, provided such persons (i) do not receive any compensation in connection with the Rule 506 offering, (ii) do not take custody of customer funds, and (iii) are not subject to a statutory ‘bad boy’ disqualification. The SEC must adopt rules to implement this part of the JOBS Act within 90 days.

CROWDFUNDING

Crowdfunding has been added to the list of “exempt transactions” under Section 4 of the Securities Act, which lists specific types of transactions that do not have to be registered under the Securities Act. Crowdfunding is a method to raise small amounts of money from a large network of investors, which is frequently done over the internet. This new exemption (the implementation of which is subject to SEC rulemaking that is due within 270 days) provides that domestic non-public issuers can raise up to \$1 million in any 12 month period through the use of either a registered broker or a new SEC registered crowdfunding portal. The maximum amount that can be sold to any investor in any 12 month period is (i) the greater of \$2,000 or 5% of the annual income or net

¹ Companies engaged in private placement offerings customarily have potential investors complete a subscription agreement or investor questionnaire, which provide that the investors make certain representations relating to their financial sophistication and accredited investor status.

worth of an investor who has an annual income or net worth of less than \$100,000, and (ii) the lesser of \$100,000 or 10% of the annual income or net worth of an investor who has an annual income or net worth equal to or more than \$100,000. Issuers will be required to provide certain information as required by the SEC for investor protection, which shall include (among other required disclosures) certain financial information, information on targeted offering amount, price, and deadline, information on management and directors, and a description of the business and business plan. Securities offered under this exemption will be “covered securities” and not subject to state “blue sky” regulation, although such securities will be subject to state antifraud rules and regulations and for one year from purchase will be subject to certain restrictions on transfer.

THRESHOLD TRIGGERING REGISTRATION UNDER THE EXCHANGE ACT

The JOBS Act amends Section 12(g) of the Exchange Act by raising the number of shareholders threshold that triggers public company reporting. Previously, Section 12(g) and Rule 12g-1 required a private company having \$10 million in total assets and at least 500 shareholders to register under the Exchange Act. Exchange Act registration subjects companies to periodic reporting (Form 10-Ks, Form 10-Qs, and Form 8-Ks), proxy rules and other disclosure requirements. The JOBS Act raises this threshold so that Exchange Act registration is required only if a company has assets in excess of \$10 million and 2,000 shareholders of record (or 500 shareholders of record who are not accredited investors). As a result, companies and private funds that wish to stay private can now accept more investors without fear that they will accidentally trigger public company

reporting requirements. In addition, the JOBS Act exempts two special groups of investors from the 2,000 shareholder calculation: (1) employees who obtained company securities under an employee compensation plan, and (2) shareholders who purchased company securities pursuant to the JOBS Act crowdfunding exemption. Therefore, the number of investors allowed under Section 12(g) can be extended even further, which will provide companies looking to grow greater flexibility in raising capital.

ADDITIONAL INFORMATION

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