

# **JOBS Act: Providing Flexibility for “Emerging Growth Companies”**

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On April 5, 2012, President Obama signed the Jumpstart Our Business Startups Act (the “JOBS Act”) into law to try to facilitate capital raising by reducing regulatory burdens on smaller companies. Among other things, the JOBS Act creates a new category of issuer, the “Emerging Growth Company,” reduces the burdens associated with the IPO process for Emerging Growth Companies, allows for general advertising and general solicitation in Regulation D offerings to accredited investors, raises the limit for Regulation A offerings from \$5 million to \$50 million, creates a new “crowdfunding” exemption, and raises the shareholder threshold for public company reporting requirements under the Securities Exchange Act of 1934, as amended (the “Exchange Act”).

This news alert summarizes certain key provisions of the JOBS Act. While certain provisions of the JOBS Act became effective upon enactment, others will not become effective until the Securities and Exchange Commission (the “SEC”) issues implementing rules.

## **Emerging Growth Companies**

The JOBS Act eases certain IPO offering and reporting requirements for a new category of issuer, the Emerging Growth Company. An Emerging Growth Company is defined as an issuer that had total annual gross revenues of less than \$1 billion during its most recently completed fiscal year. Only issuers that completed an IPO after December 8, 2011 may qualify as an Emerging Growth Company.

Issuers qualifying as Emerging Growth Companies maintain such status until the earliest of:

- the last day of the fiscal year in which the issuer had gross revenues exceeding \$1 billion;
- the last day of the fiscal year following the fifth anniversary of the effective date of the issuer’s registration statement;
- the date on which the issuer has, during the previous three-year period, issued non-convertible debt securities exceeding \$1 billion; or
- the date on which the issuer qualifies as a “large accelerated filer.”

## **Initial Public Offerings**

The JOBS Act is likely to impact IPOs in the United States because the majority of issuers conducting IPOs will qualify as Emerging Growth Companies and, therefore, be eligible for various exemptions and relaxed regulatory requirements. For instance, according to Dealogic, in 2011, 98 of 107 companies that conducted IPOs in the United States had less than \$1 billion in revenue (only includes deals for which revenue was available), and would have qualified as Emerging Growth Companies as defined by the JOBS Act.<sup>1</sup>

Emerging Growth Companies will be allowed to:

- submit a draft registration statement for confidential nonpublic review, provided that the submission must be publicly filed with the SEC not later than 21 days before the date on which the issuer conducts a road show (draft registration statements should be submitted in paper or in text searchable PDF format on a CD/DVD and accompanied by a transmittal letter confirming the issuer’s status as an Emerging Growth Company);
- engage in oral or written communications, either before or after the filing of a registration statement, with investors that qualify as accredited investors or qualified institutional buyers;
- present two years, rather than the previously required three years, of audited financial statements in the issuer’s IPO registration statement;
- exclude from the issuer’s IPO registration statement selected financial data for any period prior to the earliest audited period presented in its IPO registration statement; and
- comply with the executive compensation disclosures applicable to smaller reporting companies.

In addition to the above, Emerging Growth Companies will not be required to:

- comply with any new or revised financial accounting standard until private companies are required to comply with such new or revised accounting standard;
- obtain auditor attestation report of internal control assessments as required pursuant to Section 404(b) of the Sarbanes-Oxley Act of 2002 and related SEC rules;
- hold non-binding shareholder votes on say-on-pay and say-on-frequency; or
- disclose certain golden parachute compensation arrangements.

### **Private Placements**

The JOBS Act eases the solicitation and advertising requirements of Rule 506 of Regulation D and Rule 144A of the Securities Act of 1933, as amended (the “Securities Act”), applicable to certain private securities offerings. The JOBS Act permits general solicitation and general advertising for offers and sales of securities made pursuant to Rule 506, provided that all purchasers of such securities are accredited investors. The JOBS Act also provides that no person shall be subject to the broker or dealer registration requirements of Rule 506 solely because that person maintains a platform or mechanisms permitting the offer or sale of securities, general solicitations, general advertisements, or similar activities by issuers of such securities, whether online, in person or through any other means. Similarly, the JOBS Act permits general solicitation and general advertising for offers and sales of securities made pursuant to Rule 144A, provided such securities are only sold to persons the issuer reasonably believes to be a qualified institutional buyer.

The SEC is required to revise Rule 506 and Rule 144A within 90 days of the enactment of the JOBS Act in order to implement these changes.

### **Exempt Offerings**

The JOBS Act creates the following new categories of exempt offerings:

#### **a. Exemption for Offerings of Less than \$50 Million**

The JOBS Act requires the SEC to establish an exempt class of securities under Regulation A for offerings with an aggregate amount of up to \$50 million, increased from the previously prescribed \$5 million offering amount, offered and sold within a 12-month period. This exemption will only apply to equity securities, debt securities and debt securities convertible into or exchangeable for equity interests, including any guarantees of such securities. Securities meeting these requirements will be permitted to be offered and sold publicly and will not constitute restricted securities within the meaning of the Federal securities laws. The JOBS Act requires the SEC to adopt rules implementing these provisions, although no time frame is established.

#### **b. Crowdfunding Exemption**

The JOBS Act also creates a new exemption for capital raised by companies using “crowdfunding” efforts. Crowdfunding describes offerings to a large group of investors who each make limited investments in a company (e.g. via the Internet). A company can rely on the crowdfunding exemption if the following conditions are met:

- the aggregate amount sold to all investors during the 12-month period preceding the date of the transaction is not more than \$1 million;
- the aggregate amount sold to any investor during the 12-month period preceding the date of the transaction does not exceed:
  - the greater of \$2,000 or 5% of the annual income or net worth of the investor if either the annual income or the net worth of the investor is less than \$100,000; and
  - 10% of the annual income or net worth of the investor, not to exceed a maximum aggregate amount sold of \$100,000, if either the annual income or net worth of the investor is equal to or more than \$100,000; and
- the transaction is conducted through a broker or funding portal that complies with certain Securities Act requirements, such as registering with the SEC as a broker or funding portal, registering with any applicable self-regulatory organization and providing disclosures as determined by the SEC.

Issuers that offer and sell securities pursuant to the crowdfunding exemption will be required to:

- file with the SEC and provide the following to investors and the relevant broker or funding portal:
  - certain information about the issuer, including the names of officers and directors of the issuer;

- a description of (i) the business of the issuer and the anticipated business plan of the issuer; (ii) the financial condition of the issuer; (iii) the stated purpose and intended use of the proceeds of the offering; and (iv) the ownership and capital structure of the issuer;
  - the target offering amount and the deadline to reach such amount;
  - the price to the public of the securities or the method for determining the price;
- refrain from advertising the terms of the offering, except for notices that direct investors to the funding portal or broker;
- refrain from compensating any person to promote the offering through communication channels provided by a broker or funding portal; and
- file with the SEC and provide to investors, not less than annually, reports of the results of operations and financial statements of the issuer, as shall be determined by the SEC.

### Shareholder Threshold For Registration

The JOBS Act raises the shareholder threshold for public company reporting requirements under the Exchange Act. Pursuant to the JOBS Act, an issuer is required to file a registration statement with the SEC with respect to the sale of securities within 120 days after the last day of its first fiscal year ended on which the issuer has total assets exceeding \$10,000,000 and a class of equity security (other than an exempted security) held of record by either (i) 2,000 persons or (ii) 500 persons who are not accredited investors. Prior to the enactment of the JOBS Act, companies with total assets exceeding \$10,000,000 and a class of equity security held of record by 500 or more persons were required to register as public companies with the SEC.

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<sup>1</sup>See Andrew Ackerman and Lynn Cowan, *Jobs Bill Loosens IPO Regulations*, The Wall Street Journal (Mar. 8, 2012)

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