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Final JOBS Act Signed: Significant Reform Impacts Small Business

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President Obama signed into law yesterday the Jumpstart Our Business Startups Act (the "JOBS Act"), which was passed with overwhelming support by both the Senate and the House of Representatives. The JOBS Act includes far-reaching reforms that will significantly expand the options small businesses have to raise capital and reduce the burden of the securities offering process for early-stage companies. The principal features of the legislation are summarized below.

Reduced Regulatory Burden for Emerging Growth Companies

The JOBS Act recognizes the "emerging growth company" as a new category of issuer. An emerging growth company is generally a company that had less than $1 billion in gross annual revenue during its most recent fiscal year. A company will continue to be an emerging growth company until the earliest of (i) the last day of the first fiscal year in which annual gross revenue exceeds $1 billion; (ii) the last day of the first fiscal year following the fifth anniversary of its first sale of common equity securities pursuant to an effective registration statement under the Securities Act of 1933 (the "Securities Act"); (iii) the date on which it has issued more than $1 billion in non-convertible debt during the preceding three-year period; and (iv) the date it becomes a "large accelerated filer" as defined in Rule 12b-2 under the Securities Exchange Act of 1934 (the "Exchange Act") (which would generally occur once the emerging growth company has a market capitalization of $700 million and 12 months of reporting history as a public company). A company that completed its initial public offering on or prior to December 8, 2011 cannot be an emerging growth company.

An emerging growth company is permitted in connection with its initial public offering to:

- submit a draft registration statement confidentially to the SEC and engage in the comment process outside the public view provided that the initial confidential submission and all amendments are publicly filed at least 21 days before the commencement of the roadshow;

- hold meetings and engage in written communications with qualified institutional buyers and institutional accredited investors, both prior to filing and during the SEC's review of the registration statement, to "test the waters" and determine the level of interest in the proposed initial public offering without violating gun-jumping restrictions; and

- provide two years rather than three years of audited financial statements in S-1 or F-1 registration statements (and will not be required to include selected financial data for

periods prior to the earliest audited financial statements included in the registration statement; current regulations require inclusion of up to five years of selected financial data).

In addition, an investment bank engaged as an underwriter for an initial public offering by an emerging growth company may publish research reports prior to and after commencement and effectiveness of the offering without having such research reports be deemed an offer to sell securities. The JOBS Act prohibits the SEC and national securities exchanges from restricting a securities analyst from meeting with the management of an emerging growth company, even if the meeting is attended by personnel from other functional areas within the investment bank. The JOBS Act also prohibits the SEC and national securities exchanges from restricting the publication of research reports regarding an emerging growth company during any prescribed period of time following the initial public offering date or prior to the expiration of IPO-related lock-up agreements.

The IPO-related reforms for emerging growth companies will permit emerging growth companies to avoid disclosing sensitive business information to the market prior to the time the efficacy of an initial public offering has been confirmed and may also allow emerging growth companies to avoid the adverse consequences of abandoning an offering that has been publicly announced.

A number of significant accounting and disclosure requirements are inapplicable to emerging growth companies for so long as they retain emerging growth company status:

- emerging growth companies will not be required to provide an auditor attestation on management's assessment of internal controls under Section 404(b) of the Sarbanes-Oxley Act of 2002 (the CEO and CFO of an emerging growth company will, however, be required to certify as to internal controls in periodic reports as otherwise required under the Sarbanes-Oxley Act);

- emerging growth companies will not be required to hold "say-on-pay," "say-on-frequency" or "say-on-parachute" shareholder advisory votes on the compensation of named executive officers as required by the Dodd-Frank Act of 2010;

- emerging growth companies are exempt from certain disclosure requirements relating to executive compensation and generally may comply with the compensation disclosure requirements applicable to a "smaller reporting company," as defined in Rule 12b-2 under the Exchange Act;

- emerging growth companies will not be subject to any PCAOB rules regarding mandatory audit firm rotation or the inclusion in the audit report of information about the audit and financial statements of the issuer (co-called auditor discussion and analysis); and emerging growth companies will not be subject to any other future PCAOB rules

unless the SEC determines that application is in the public interest after consideration of investor protection and the promotion of efficiency, competition, and capital formation; and

- emerging growth companies will not be required to comply with new or revised U.S. GAAP accounting pronouncements until the pronouncements become applicable to private companies (but if they elect to comply with public company accounting standards they may not do so selectively).

The JOBS Act requires the SEC to conduct a review of Regulation S-K and report to Congress within 180 days after enactment of the JOBS Act with proposals to update, modernize, and simplify offering-related and periodic disclosure requirements for emerging growth companies.

Increased Threshold for Public Company Reporting

The JOBS Act increases the shareholder threshold at which private companies are required to register a class of securities under the Exchange Act, and therefore become subject to public company reporting requirements, from 500 to 2,000 shareholders of record, exclusive of securities received under employee compensation plans and securities issued in crowdfunding transactions (discussed below), as long as not more than 499 shareholders are unaccredited. The asset threshold is increased from $1 million to $10 million.

Other Rule Changes Encouraging Small Company Capital Formation

Increase in Offering Limit under Small Issue Exemption. The JOBS Act authorizes, and directs the SEC to add by rule or regulation, a small issue registration exemption for equity, debt and convertible debt securities of up to $50 million in any 12-month period, an increase from the existing $5 million limit on small issue exemptions under Section 3(b) of the Securities Act. Securities issued under the enhanced exemption will be unrestricted and may be publicly offered. Issuers will be required to file audited financial statements with the SEC annually, and the SEC may impose a requirement to file and distribute an offering statement including audited financial statements as a condition to the exemption. The SEC may by future rulemaking also impose periodic reporting requirements on issuers availing themselves of the exemption. Offerings under the enhanced small issue exemption will be subject to state securities laws unless they are sold on a national exchange or to qualified purchasers.

General Solicitations to Accredited Investors and Qualified Institutional Buyers. The JOBS Act directs the SEC, within 90 days of enactment, to revise its rules to permit general solicitation and advertising in connection with the private placement of securities under Rule 506 of Regulation D, as long as the purchasers are all accredited investors, and under Rule 144A, as long as the purchasers are all reasonably believed to be qualified institutional buyers. This change will greatly expand the marketing channels available to private issuers seeking to raise

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capital under these rules. Among other things, the new rules, when issued, will permit a private placement to be conducted concurrently with a public offering even if purchasers in the private placement are not committed to purchase prior to the time a registration statement is filed.

The JOBS Act also amends the Securities Act of 1933 to exempt persons operating trading platforms for the sale of securities in a Rule 506 private placement from broker-dealer registration provided that such persons receive no compensation in connection with the purchase or sale of securities and are not subject to a statutory disqualification and that the platform does not have possession of customer funds or securities.

Crowdfunding. The JOBS Act creates new Section 4(6) of the Securities Act to facilitate so-called crowdfunding, a technique for raising capital in small individual amounts. The JOBS Act limits the aggregate dollar amount of securities that an issuer can sell in a crowdfunding transaction to $1 million over a 12-month period. The amount that an issuer can sell to an individual investor in any 12-month period is limited to the maximum of (i) the greater of $2,000 and 5% of the annual income or net worth of an investor, if either the investor's net worth or annual income is less than $100,000; and (ii) 10% of an investor's annual income or net worth, but not in excess of $100,000, if either the investor's annual income or net worth is equal to or greater than $100,000. Investors in a crowdfunding need not be accredited investors. Issuers will be required to file specified information with the SEC and provide such information to investors and will also have ongoing reporting requirements concerning the crowdfunding. Securities issued in a crowdfunding may not be transferred for one year after purchase, subject to limited exceptinos.

A broker or funding portal must be used as an intermediary under the crowdfunding exemption. The broker or funding portal will be required to register with the SEC and will be responsible to, among other things, ensure that investors understand the risks of and meet certain suitability standards for the investment; monitor investment limits; and conduct due diligence on the principals of the issuer. No advertising is permitted other than notices directing investors to the broker or funding portal.

The SEC is directed to adopt regulations required to implement the crowdfunding exemption within 270 days of enactment of the JOBS Act.

For additional guidance on how the JOBS Act may impact your capital raising requirements, contact your regular Akerman attorney or a member of the firm's securities practice.