



Checklist for Issuers of Private Placements under Regulation D, Rule 504, 505, and 506

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September 8, 2011

While the Internet has turned into a ubiquitous resource for information on private placements and the creation of private placement memoranda, information outlining the issues that need to be addressed before and after the completion of a private placement memorandum is still relatively hard to come by.

It's therefore no surprise that many issuers, especially those who take it upon themselves to create the required framework for their offering, are misinformed and unaware of the additional tasks and processes required to develop a workable Regulation D offering and thus, preserve the exemption afforded under state and federal securities laws.

This article is designed to serve as a practical guide and reference for issuers who are contemplating, preparing for, or already working on an exempt offering of restricted and unregistered securities under Regulation D. While this article is intended to be complete, it may not apply in its entirety to every issuer.

1. Preliminary Considerations

- 1.1. Fundamentals supporting current financing objectives;
- 1.2. Background of officers, directors, general partners and managing member of the issuer, including shareholders owning/controlling an equity position of 10% or more, to comply with current and proposed bad actor disqualification requirements. See our article at: <http://publications.jacksonsteiner.com/article/sec-proposes-rule-banning-bad-actors-from-private-placements-under-regulation-d-rule-506>;
- 1.3. Offering details
 - 1.3.1. Offering type (e.g. equity, debt, hybrids, or other securities);
 - 1.3.2. Offering framework such as exempt offerings under Regulation D, Rule §504, §505 or §506 (safe-harbor), intra-state or other offering structures that may require registration. See our article "Introduction to Private Placements under Regulation D" at <http://publications.jacksonsteiner.com/article/introduction-to-private-placements-under-regulation-d> to create a starting point for discussions with your team and legal counsel.
 - 1.3.3. Consult with legal counsel to (i) discuss offering type and structure to determine potential state Blue Sky filing requirements and (ii) potential exposure to and compliance with bad actor disqualification requirements.

- 1.3.4. Consult with financial advisor or investment banking professional to balance legal concerns with financing objectives and capital market insights.
- 1.3.5. Offering amount;
- 1.3.6. Valuation;
- 1.3.7. Pricing of securities;
- 1.3.8. Minimum offering required to break escrow;
- 1.3.9. Distribution strategy for securities;
- 1.3.10. Relationships with broker-dealers, finders, and other intermediaries;
- 1.3.11. Hire escrow agent (discuss with your bank, consider costs);
- 1.3.12. Offering schedule;
- 1.3.13. Shareholder-, committee- or board meeting to approve offering;

2. Construct Offering

- 2.1. Review and update business plan
 - 2.1.1. Review, analyze, and update business strategy and overall outlook;
 - 2.1.2. Review, analyze, and update financial statements and financial forecast;
 - 2.1.3. Consider developing a business plan in support of the offering and assist in the development of the company sections for your private placement memorandum.
- 2.2. Retain legal counsel and/or financial services firm to assist you with the development of your offering and private placement memorandum.
- 2.3. Review a sample private placement memorandum. Seeing how others constructed their offering may offer valuable insights into what information you will need to gather and how it will be presented in your private placement memorandum. There is a sample private placement memorandum for a Regulation D offering under Rule 506 available as a free download at: <http://publications.jacksonsteiner.com/free-sample-private-placement-memorandum-reg-d-rule-506>. If you require a sample private placement memorandum, specific to your industry or line of business, or if you plan adopting another rule, check <http://publications.fastventures.com/reference-documents>.
- 2.4. Develop private placement memorandum
 - 2.4.1. Create a workgroup, including members of your team, legal counsel, and financial advisor/investment banking professional to construct your offering and develop a corresponding private placement memorandum.
 - 2.4.2. Review, analyze, and update the document after completing every major milestone.
 - 2.4.3. Discuss the final draft of the document on with your team to make sure every team member is up to date and prepared to fulfill his function during the subsequent solicitation phase.
 - 2.4.4. Consider developing a so-called road show (e.g. Power Point® presentation) to spark the interest of intermediaries (e.g. broker dealers, attorneys, and other gate keepers) and potential investors. It's a good conversation starter.
 - 2.4.5. If your team doesn't include legal counsel as of yet, retain counsel now to (i) review your private placement memorandum including purchaser questionnaires and subscription agreement, along with the proposed securities distribution strategy, (ii) ensure compliance with state Blue Sky filing requirements, if applicable, and (iii) ensure compliance with bad actor disqualification requirements.

3. Prepare for Due Diligence

While almost every investor has his own way to conduct due diligence on a potential investment opportunity, issuers should adequately prepare for this key event and be able to turn around requests for additional information based on very little lead time. Information and supporting documents investors typically request while conducting due diligence are listed below:

3.1. Organizational Structure and Certificate of Good Standing

- 3.1.1. Certificate of Incorporation, as amended;
- 3.1.2. By-Laws;
- 3.1.3. Shareholder- or Partnership Agreement;
- 3.1.4. Certificate of Good Standing (long form);
- 3.1.5. Tax Status Certificate;
- 3.1.6. List of states where company has offices and thus, is or should be qualified as a foreign entity doing business in that state. Secure Certificate of Good Standing, and Tax Status Certificate for these states as well, if applicable.
- 3.1.7. Corporate minutes and stock register, including minutes of board of directors and executive meetings and other committees.
- 3.1.8. Strategic partnership- and/or joint venture agreements, if applicable.

3.2. Shareholders & Capitalization

- 3.2.1. List of shareholders, cross-checked against stock register;
- 3.2.2. List of shareholders with special status, (e.g. trustees, etc.);
- 3.2.3. Trust agreements, if shares are held in a fiduciary capacity;
- 3.2.4. Preemptive rights confirmation;
- 3.2.5. ESOP (Employee Stock Ownership Plan), stock option and other agreements requiring the issuance of stock;
- 3.2.6. Letter from accountant or auditors confirming fully paid and non-assessable shares and corresponding accounting methods;
- 3.2.7. Power of attorney and stock escrow agreements;

3.3. Corporate Resolutions, Authorization

- 3.3.1. Review stockholder approvals of previous transactions;
- 3.3.2. Review any other agreements or resolutions governing the issuance of stock;
- 3.3.3. Confirm corporate or fiduciary powers to approve offering;
- 3.3.4. Evaluate voting trusts, outstanding proxies or other agreements governing voting;
- 3.3.5. Review restrictive share transfer agreements, obtain legal opinion to ensure compliance;

3.4. Financial Statements

- 3.4.1. Two to three years' worth of audited financial statements with access to auditors and their work papers, if applicable;
- 3.4.2. Most-recent financial statements (unaudited), comparable statements for prior fiscal year;
- 3.4.3. All financial projections;
- 3.4.4. Auditors' letter to management for two years, if applicable;
- 3.4.5. Auditors' inquiries and management's replies for two years;
- 3.4.6. Review of accounts receivables (quality of individual accounts, aging, special cases);
- 3.4.7. Review of inventory;
- 3.4.8. Review and analysis of SG&A (Selling, General & Administrative Expenses);
- 3.4.9. Obtain corporate credit reports;
- 3.4.10. Order backlog;

- 3.5. Tax Filings (Federal & State)
 - 3.5.1. Copies of corporate tax return for latest closed and all open years (i.e. federal, state, and local);
 - 3.5.2. Reports for IRS audits, if any;
 - 3.5.3. Settlement agreements with IRS and state tax authorities, if any;
 - 3.5.4. Agreements to waive statute of limitations or extending time to examine;
- 3.6. Employee Matters, Benefit Plans, Compensation, Labor Disputes
 - 3.6.1. Executive and employment agreements;
 - 3.6.2. Non-Disclosure- and Non-Compete Agreements;
 - 3.6.3. Confirm assumptions for pension plans and actuarial reports;
 - 3.6.4. Profit-sharing agreements;
 - 3.6.5. ESOP (Employee Stock Ownership Plan) and stock option bonus plans and agreements;
 - 3.6.6. Calculation of fund assets and liabilities;
 - 3.6.7. Fringe benefits, holidays, and vacations granted to employees;
 - 3.6.8. Report on labor disputes, requests for arbitration, grievance proceedings, etc.;
 - 3.6.9. Report on employees, turnover, and absentee history;
- 3.7. Other Contracts
 - 3.7.1. All loan agreements (e.g. loans provided by (i) banks, (ii) the Small Business Administration, (iii) shareholders, and (iv) suppliers, along with loans provided to (i) key customers (ii) shareholders, and (iii) employees.
 - 3.7.2. Customer credit and installment payment agreements above designated dollar amount;
 - 3.7.3. UCC (Uniform Commercial Code) statement search in relevant states;
 - 3.7.4. Customer list;
 - 3.7.5. Deeds;
 - 3.7.6. Leases;
 - 3.7.7. Contracts with insiders or other contractual arrangements;
 - 3.7.8. Membership agreements or relations with trade associates;
 - 3.7.9. Review of terms for contracts being assumed or continued;
 - 3.7.10. Guarantees;
- 3.8. Licenses
 - 3.8.1. Business licenses;
 - 3.8.2. Registration with federal, state, and local authorities if operations require registration;
 - 3.8.3. Material licensing agreements granted to and by the company;
- 3.9. Insurance
 - 3.9.1. Insurance policies (e.g. business interruption, liability);
 - 3.9.2. Key man life insurance and present value calculation;
 - 3.9.3. Provide letter or report from carrier concerning continuing coverage;
 - 3.9.4. Workers' compensation;
- 3.10. Litigation
 - 3.10.1. Complete list and evaluation of threatening and ongoing litigation;
 - 3.10.2. Contact list for legal counsel;
 - 3.10.3. Judgment searches in relevant states;
 - 3.10.4. Insurance coverage for threatening and ongoing litigation;
 - 3.10.5. Regulatory compliance (e.g. FTC, FDA, OSHA, EPA, HIPAA, EEOC, SEC, etc.);
- 3.11. Patents and Trademarks
 - 3.11.1. List and status report for all patents;

- 3.11.2. List and status report for all trademarks (including continuation notices);
- 3.11.3. List of copyrighted material;
- 3.11.4. Examination of common-law protection;
- 3.12. Properties
 - 3.12.1. Title reports and insurance policies;
 - 3.12.2. UCC searches in relevant states;
 - 3.12.3. Condition of plant, machinery, and other equipment;
 - 3.12.4. Assessment of energy costs and possible strategies to convert to green energy;

4. Soliciting Investors

- 4.1. Warm-up potential investors on your shortlist;
- 4.2. Consider strategic partnerships with broker-dealers, intermediaries, and quality prospecting services (yes, there are a few reputable ones; that even industry titans such as Blackstone® uses to supplement their own lead generation).
- 4.3. Develop a structured prospecting strategy. Many issuers will likely face serious doubts on where to look for investors, how to approach them, and how to pitch their offerings without violating state and federal securities laws (i.e. no general solicitation). Fast Ventures' white paper "How to Reach High-Net-Worth Individuals with Your Private Placement or Regulation D Offering" can create a good starting point for discussions with your team level and legal counsel to determine the most suitable course of action. It offers valuable insights into research and marketing techniques that are used by major money managers to identify high-net-worth and ultra-high-net-worth individuals in any given area, approach them in compliance with federal, state, and local laws, and pitch their offerings to them. The paper is available at <http://publications.fastventures.com/reaching-high-net-worth-individuals-with-your-private-placement>.
 - 4.3.1. Identify and research local high-net-worth individuals based on the main pillars for private wealth creation (i) real estate, (ii) sale of business, (iii) stock transactions, (iv) income, and (v) inheritance.
 - 4.3.2. Pre-qualify leads as "Accredited Investor" or "Sophisticated Investor" using suitability questionnaires depending on what rule you adopted for your offering.
 - 4.3.3. Supply pre-qualified leads with a numbered copy of your private placement memorandum bearing the name of the addressee. Log every copy sent out to pre-qualified leads into a register. If a prospect is no longer interested in discussing a potential investment, ask him to return his copy of your private placement memorandum and update register accordingly. Destroy copy of private placement memorandum upon receipt. Do not recycle.
 - 4.3.4. Invite qualified leads to a meet and greet, an individual presentation, or seminar,

5. Closing

- 5.1. Schedules and agreements to be made available to subscribers upon request
 - 5.1.1. Employment agreements;
 - 5.1.2. Escrow agreements;
 - 5.1.3. Certified Certificates of Incorporation
 - 5.1.4. Certified By-Laws
 - 5.1.5. Certified shareholder or partnership agreement
 - 5.1.6. Certificates of Good Standing
 - 5.1.7. Tax Status and Lien Docket Certificates
 - 5.1.8. Certified Corporate Resolutions
 - 5.1.9. Assignments, if applicable

- 5.1.10. Schedule of all patents, trademarks, and copyrights
- 5.1.11. Schedule of all bank accounts
- 5.1.12. Legal opinions issued by legal counsel, rulings and opinion letters issued by the SEC, state regulators, and other government agencies, if applicable.
- 5.2. Final review of subscriptions
 - 5.2.1. Final review of subscription documents furnished by subscriber to issuer (e.g. subscription agreement and purchaser questionnaire(s))
 - 5.2.2. Final cross-check of subscription documents against payment held in escrow
- 5.3. Executing stock purchase agreement

6. Post-Closing

- 6.1. Issuing stock certificates to subscribers to the offering
- 6.2. Filing of Form D with the Securities & Exchange Commission
- 6.3. Releasing offering proceeds from escrow account to issuer's checking account – subject to minimum offering requirements

7. Other Matters

- 7.1. Consider creating a designated file for each subscriber to your offering within which all offering related information is retained for at least five years following the closing. Documents to be retained include but are not limited to (i) all correspondence with the subscriber, (ii) inquiries and requests for information, (iii) documents evidencing that subscriber was supplied with substantive disclosure document (i.e. private placement memorandum), (iv) signed investor suitability questionnaire evidencing subscriber's status as accredited or sophisticated investor, (v) subscription agreement, (vi) documents evidencing payment of amount subscribed to, (vii) invitation to annual shareholder meetings, (viii) reports on financial performance and dividend allocation, and (iv) copies of documents reflecting allocation/payment of dividends and/or other payments.

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