Keeping Two Offerings from Being One Illegal One – Bruce E. Methven

If a company makes two securities offerings too close together, the securities regulators may consider the two offerings “integrated”, meaning two parts of a single offering. That can violate the requirements of the securities exemptions being used, making the offerings illegal.

This happens because many securities exemptions have restrictions on the types of investors, the number of investors, the amount of money being raised or the advertising that’s allowed. For example, a Rule 506 offering is allowed only 35 non-accredited but sophisticated investors. Imagine one offering has 20 sophisticated investors and a closely following second Rule 506 offering has 25 investors. The regulators may consider the two offerings “integrated” (as one offering) with 45 sophisticated investors so that it violates the limit of 35. That means that the offerings have been made in violation of the securities laws.

The same thing can happen, for example, with an offering under the Model Accredited Investors Exemption, which allows a brief public “tombstone” ad. If it is followed too closely by another offering that does not allow any public advertising (such as the traditional Rule 506 offering), there is a securities violation.

Fortunately there is a “safe harbor”: If there are at least six months between the end of one offering and the beginning of the other, two offerings will not be integrated. Given this, offering companies want to either 1) make sure that their offerings are at least six months apart or 2) plan their offerings carefully so that even taken together the exemption requirements are not violated. In the first example above, that might mean limiting sophisticated investors in the second offering to 15 non-accredited but sophisticated investors.

There is a similar issue concerning the new crowdfunding exemption under the JOBS Act. Under Section 302(6)(A) the total amount sold to all investors, including but not limited to the crowdfunding exemption during the 12-month period preceding the crowdfunding offer, cannot more than $1,000,000. That means that a company that has already raised $500,000 in the last 12 months from any type of offering can only raise $500,000 in a crowdfunding offer. The restriction also applies to an affiliate of the offeror – an entity “under common control with the issuer” – such as a parent company, subsidiary or sister company. This $1,000,000 limitation is one of the things that a crowdfunding intermediary is required to track.

Still, for the most part, a bit of planning can remove the danger of violating the integration rule.

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