

JOBS Act – Small Company Capital Formation – Regulation A+

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On April 5, 2012, President Obama signed the JOBS Act, the culmination of a bipartisan effort by Congress to ease restrictions on capital raising that have affected and guided companies and investors for decades. The Act, among other things, creates a new exemption from registration under the Securities Act of 1933, colloquially known as “Regulation A+”.

Perspective on Small Issue Exemption

Before there was Regulation A+, there was Regulation A. Since 1933, Regulation A facilitated public financing by small businesses by exempting limited issuances of securities from registration under the Securities Act and its prospectus and registration statement requirements. Regulation A includes a set of substantive disclosures for an issuer, its business and its finance. The maximum amount of an offering pursuant to Regulation A has increased over time, reflecting both changes in the value of the dollar and Congress’ evolving approach on easing access to capital for smaller companies, as follows:

- \$100,000 – 1933
- \$300,000 – 1945
- \$500,000 – 1970
- \$1,500,000 – May, 1978
- \$2,000,000 – October, 1978
- \$5,000,000 – 1980

What Is Regulation A+ ?

The JOBS Act directs the SEC to amend Regulation A (or adopt a similar exemption) to permit issuers to raise up to \$50 million in aggregate from the sale of securities in any 12-month period in reliance on the exemption. The previous Regulation A limitation was only \$5 million. The SEC is also directed to review the \$50 million offering amount limitation and increase this amount every two years, or report on its reasons for not increasing the amount.

Regulation A+ applies to equity, debt or convertible securities. Securities sold pursuant to Regulation A+ will not be restricted securities and may be immediately resold. Securities sold pursuant to Regulation A+ are “covered securities” for purposes of the National Securities Markets Improvement Act of 1996, and therefore substantive state “blue sky” regulation is preempted. Regulation A+ securities may be offered and sold publicly, so long as the securities are offered or sold on a national securities exchange, or offered or sold to “qualified purchasers” (as the SEC determines).

Regulation A+ will require the filing of an offering circular with the SEC, but this disclosure will be far less onerous, and inexpensive, than the disclosures required of a traditional IPO. An issuer will be permitted to “test the waters” and solicit interest in its securities before filing the offering circular in order to gauge interest in the securities before bearing the expense of Regulation A+ compliance.

The Regulation A+ provision of the JOBS Act adopts several investor protection measures, including the civil liability provision of the Securities Act (Section 12(a)(2)) for false or misleading statements or omissions in connection with the offer or sale of securities, and will require filing of the issuer’s audited financial statements with the SEC annually. The SEC is authorized to prescribe rules requiring periodic

disclosures including a description of the issuer's business operations, its financial condition, its corporate governance principles, its use of investor funds, and other related information. The SEC may also promulgate disqualifications provisions to exclude "bad actors" from the use of Regulation A+.

The JOBS Act establishes no deadline for the SEC to adopt corresponding rules regarding Regulation A+. Therefore, issuers and securities practitioners must wait for the forthcoming SEC rules to actually utilize Regulation A+.

What May Now Be Different for Companies and Entrepreneurs Moving Forward?

The Regulation A exemption was rarely used because it had a low maximum offering and was perceived as cumbersome. Now that Regulation A+ authorizes offerings up to \$50 million, it may be seen as a viable alternative to Rule 506 and Regulation D - the dominant exemption for private companies raising capital. Regulation A+ differs from Rule 506, because

- Regulation A+ allows for sales to non-accredited investors;
- Securities issued under Regulation A+ are not "restricted"; and
- Under Regulation A+ securities may be offered and sold publicly.

The Regulation A+ exemption may be viewed as an issuer friendly statute requiring only limited disclosure in exchange for the opportunity to sell up to \$50 million in unrestricted securities to the general public. Compliance with Regulation A+'s offering circular, financial and other disclosure requirements may be considered a dress rehearsal for a full-blown registered public offering for later-stage companies. The tenfold increase in maximum offering amount to \$50 million warrants substantial consideration of the use of Regulation A+ for capital formation by smaller issuers.

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