



Insights: Alerts

SEC Adopts Final Regulation A+ Rules Ushering in New Era of Capital Raising

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On March 25, 2015, the Securities and Exchange Commission (the “SEC”) adopted final rules that update and expand Regulation A under the Securities Act of 1933, as amended (the “Securities Act”), an existing exemption from registration for smaller issuers of securities. Under the current Regulation A, non-reporting companies can sell up to \$5 million of securities in a public offering without being subject to the SEC’s public company reporting regime. The final rules, often referred to as “Regulation A+,” will permit companies to offer and sell up to \$50 million of securities in a 12-month period.

Offering Tiers

Regulation A+ provides for two tiers of offerings:

- **Tier 1** – up to \$20 million in a rolling 12-month period (including no more than \$6 million on behalf of selling securityholders that are affiliates of the issuer).
- **Tier 2** – up to \$50 million in a rolling 12-month period (including no more than \$15 million on behalf of selling securityholders that are affiliates of the issuer).

In addition, sales by selling securityholders in an issuer’s initial Regulation A offering and any subsequently qualified Regulation A offering within the 12-month period following the date of qualification of the initial Regulation A offering is limited to 30 percent of the aggregate offering price.

Eligible Issuers

Regulation A+ is limited to issuers organized and having their principal place of business in the United States or Canada. The following issuers will be “ineligible” for the exemption provided under Regulation A+:

- an issuer that is an SEC-reporting company;
- a blank check company;
- any investment company registered or required to be registered under the Investment Company Act of 1940 (this includes business development companies); and
- any entity issuing fractional undivided interests in oil or gas rights, or similar interests in other mineral rights.

The exemption also is not available to issuers:

- that have not filed with the SEC the ongoing reports required by Regulation A+ during the two years immediately preceding the filing of a new offering statement;
- that have had their registration revoked pursuant to an order under Section 12(j) of the Securities Exchange Act of 1934 (the “Exchange Act”) that was entered into within five years before the filing of the offering statement; and
- subject to the bad actor disqualification.

Eligible Securities

All offerings under Regulation A+ are limited to equity securities, (including warrants), debt securities and debt securities convertible into or exchangeable into equity interests, including any guarantees of such securities. The final rules specifically exclude asset-backed securities.

Continuous Offerings

The final rules continue to permit continuous or delayed offerings in certain circumstances, providing greater flexibility to issuers with respect to the timing of their offerings. However, the final rules condition the ability to sell securities in a continuous or delayed Tier 2 offering on being current with ongoing reporting requirements at the time of sale.

Investment Limitation

The final rules impose an investment limit for Tier 2 offerings of no more than (i) 10% of the greater of the investor’s annual income and net worth (for natural persons) and (ii) 10% of the greater of annual revenue or net assets at fiscal year-end (for non-natural persons). The investment limitation will not apply to accredited investors or to securities that are to be listed on a national securities exchange at the consummation of the offering. Investors must be notified of the investment limitation. Issuers may rely on an investor’s representation of compliance with such investment limitation, unless the issuer knew at the time of sale that such representation was untrue.

Solicitation

Under Regulation A+, issuers are permitted to “test the waters” or solicit interest in a potential offering from the general public either before or after the filing of the offering statement, provided any solicitation materials used after publicly filing the offering statement are preceded or accompanied by a preliminary offering circular or contain a notice informing potential investors where and how the most current preliminary offering circular can be obtained. Solicitation materials must be filed as exhibits to the offering statement, including in connection with a submission for non-public review.

Integration of Offerings

Regulation A+ includes a safe harbor that provides that a Regulation A+ offering will not be integrated with:

- prior offers or sales of securities; or
- subsequent offers or sales of securities that are:

- registered under the Securities Act, except as provided in Rule 255(e) [abandoned offerings];
- made in reliance on Rule 701;
- made pursuant to an employee benefit plan;
- made in reliance on Regulation S [offerings outside of the U.S.];
- made pursuant to Section 4(a)(6) of the Securities Act [crowdfunded offerings]; or
- made more than six months after the completion of the Regulation A offering.

Filing Requirements

The final rules amend the filing process and add the option to submit an offering statement for non-public review by the SEC. For those issuers that choose the non-public review, the offering statement must be filed publicly not less than 21 calendar days before qualification of the offering statement. Regulation A+ offering statements, periodic reports and any other documents required to be submitted to the SEC in connection with a Regulation A+ offering must now be filed via EDGAR. The amended Form 1-A is comprised of three parts:

- Part I – requires basic issuer information, jurisdictions in which the securities will be offered, and sales of unregistered securities.
- Part II – requires basic disclosures related to the offering and the issuer, including the use of proceeds, a description of the securities being offered, issuer’s business, executive officers and directors, beneficial ownership, risk factors, financial statements (audited if Tier 2 issuer) and other disclosures. This is similar to Part I of Form S-1, which an issuer can choose to comply with in connection with the offering statement.
- Part III – requires certain exhibits and related materials.

Ongoing Reporting Obligations

Tier 1 issuers will be required to file an exit report after the completion or termination of an offering. The exit report must be provided in a Form 1-Z, which includes: the date the offering was qualified and commenced, the amount of securities qualified, the amount of securities sold in the offering, the price of the securities, the portions of the offering that were sold on behalf of the issuer and any selling securityholders, any fees associated with the offering, and the net proceeds to the issuer.

Tier 2 issuers will be subject to a number of additional reporting obligations, including:

- annual reports on Form 1-K;
- semi-annual reports on Form 1-SA;
- current reports on Form 1-U; and
- special financial reports on Form 1-K and Form 1-SA.

The Form 1-K requirements are similar in scope to the Form 1-A, including audited financial statements, and must be filed within 120 calendar days of the issuer’s fiscal year-end. The Form 1-SA requirements are similar in scope to the scaled disclosure required in a Form 10-Q and must be filed within 90 calendar days after the end of the first six months of the issuer’s fiscal year.

Tier 2 issuers may suspend or terminate their ongoing reporting obligations on a basis similar to the provisions that allow issuers to suspend their ongoing reporting obligations under Section 13 and Section 15(d) of the

Exchange Act. Regulation A+ permits a Tier 2 issuer to exit the ongoing reporting regime at any time after completing reporting for the fiscal year in which the offering statement was qualified if it has filed all required reports for the shorter of: (1) the period since the issuer became subject to such reporting obligation, or (2) its most recent three fiscal years and the portion of the current year preceding the date of filing the Form 1-Z if the securities of each class to which the offering statement relates are held of record by fewer than 300 (1,200 if the issuer is a bank or bank holding company) persons and offers or sales made in reliance on a qualified Tier 2 offering statement are not ongoing.

Offering Circular Delivery Requirements

Regulation A+ adopts an “access equals delivery” model when sales are made on the basis of offers conducted during the pre-qualification period and the final offering circular is filed and available on Edgar. Issuers are required, not later than two business days after completion of a sale, to provide purchasers with a copy of the final offering circular or a notice with the URL where the final offering circular may be obtained on EDGAR and contact information sufficient to notify a purchaser where a request for a final offering circular can be sent.

However, in the event that an issuer that is not already subject to the Tier 2 periodic reporting requirements uses a preliminary offering circular to offer securities to potential investors, the issuer will be required to deliver the preliminary offering circular to prospective purchasers at least 48 hours in advance of sales.

State Blue Sky Laws

Historically, one of the primary drawbacks of a Regulation A offering, other than the \$5 million offering limitation, was the cost and time associated with the registration and qualification requirements of state blue sky securities laws. Regulation A+ provides Tier 2 issuers preemption from the registration and qualification requirements of state blue sky securities laws for securities offered or sold to “qualified purchasers,” which are defined as any person to whom securities are offered or sold in a Tier 2 offering. However, Tier 1 offerings will remain subject to the registration and qualification requirements of state blue sky securities laws for each state in which the issuer offers and sells securities.

Key Takeaways

Whether Tier 1 offerings under Regulation A+ become a useful tool for raising capital remains to be seen. Historically, very few issuers have utilized the Regulation A exemption to issue securities. The increase in the permissible offering size from \$5 million (under the prior version of Regulation A) to \$20 million will be appealing to issuers, but the continued application of state blue sky securities laws on Tier 1 offerings reduces the attractiveness of this method of capital raising. While issuers conducting Tier 1 offerings may avail themselves of the coordinated review program developed by the North American Securities Administrators Association as it relates to state securities laws, the coordinated review program is in its infancy and may still add additional time and costs to the process.

Tier 2 offerings may be more attractive given the higher maximum offering amount of \$50 million and the preemption of state blue sky securities laws. However, the ongoing reporting obligation – though significantly less burdensome than public company reporting requirements – plus the time and expense of the Tier 2 offering process itself may cause issuers that are seeking to raise between \$20 million and \$50 million to continue to rely on Regulation D to raise such funds from accredited investors in private placement offerings.

Effective Date

The final rules will be effective 60 days following publication in the Federal Register.

To learn more and discuss the parameters of this Legal Alert, please contact any member of Kilpatrick Townsend's Financial Institutions team.

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