

REGULATION A – NOW BIGGER, BIFURCATED AND (SOMETIMES) BENEFICIAL

Regulation A, the so-called “mini IPO” exemption from registration under the Securities Act of 1933, has existed since the 1930s. An offering limit of \$5 million combined with relatively high compliance costs kept Regulation A from being a viable option for companies seeking capital, but recent changes have breathed life into Regulation A by raising the offering maximum and making other modifications.

Tier 1 Offerings and Tier 2 Offerings: The revised Regulation A (sometimes now referred to as “Regulation A Plus”) provides for Tier 1 offerings (annual limit of \$20 million) and Tier 2 offerings (annual limit of \$50 million) of equity securities, debt securities, and certain convertible debt securities.

Common Elements: Tier 1 Offerings and Tier 2 Offerings share the following similarities:

Eligible Issuers: Only American and Canadian companies may use Regulation A. Start-up companies with a business plan may use Regulation A, too. Meanwhile, issuers excluded from using Regulation A include investment companies required to register under the Investment Company Act of 1940, business development companies, blank check companies, and SEC reporting companies.

Offering Statement: Regulation A requires that an “offering statement” on Form 1-A be declared effective prior to selling any securities. An “offering statement” consists of (i) an “offering circular” that is distributed to investors and (ii) certain exhibits and other information that need only be filed with the SEC. Like a Form S-1 for an IPO but unlike a private placement memorandum in a Rule 506 offering for accredited investors only, an offering statement has certain mandated contents. Form 1-A requires, among other items, a description of the business and use of proceeds, risk factors, discussion of financial condition and operating results, key personnel biographies and information on executive compensation.

Testing the Waters: Regulation A permits general solicitations and advertising. Offers can be made to an unlimited number of persons, and issuers may solicit interest in a potential Regulation A offering from the general public either before or after the filing of the offering statement so long as any 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 may be obtained.

“Bad Actor” Disqualification: Companies that have or whose directors, officers, promoters or sellers of securities have engaged in certain fraudulent or “bad acts” are prohibited from using Regulation A.

Antifraud: Regulation A issuers must comply with the antifraud provisions of the securities laws.

Freely Tradeable Securities: Securities acquired in a Regulation A are not “restricted securities” and are freely tradeable.

Differing Elements: In addition to offering maximums, the following differences exist between Tier 1 and Tier 2 offerings although an offering of less than \$20 million may qualify as Tier 2 (and avoid qualification at the state level) so long as it meets all the requirements of a Tier 2 offering.

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Purchasers: Both “accredited investors” and unaccredited investors may participate in Tier 1 offerings. Other than for securities to be listed on a national securities exchange, Tier 2 offerings are limited to “accredited investors” or purchasers investing no more than 10% of the greater of annual income or 10% of their net worth (or net assets in the case of entity investors).

Financial Statements: Offering statements for Tier 2 Offerings must include audited financial statements (although the auditor need not be registered with the Public Company Accounting Oversight Board) where offering statements for Tier 1 offerings may include unaudited financial statements.

State Law Compliance: Tier 1 Offerings must be qualified (or exempt from qualification) under applicable state law. Tier 2 Offerings are not required to be qualified under state law although states may require notice filings and filing fees.

Periodic Reporting: Tier 2 issuers are required to file annual, semiannual and current event reports with the SEC, and annual reports must contain audited financial statements. Tier 1 issuers whose offerings have been qualified with the SEC need only file exit reports within 30 days of an offering’s termination.

Regulation A is not for every company. The rules are detailed and complex. Legal and accounting costs, while less than for a standard IPO, may be six figures for an established company although such costs will likely be substantially lower for a start-up venture. Issuers should consult closely with FisherBroyles or other experienced securities counsel before determining whether Regulation A is appropriate for their capital raising needs.

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