



**The New**  
**“Jumpstart Our Business Startups Act”:**  
**What Private Companies Need to Know**

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This afternoon President Obama signed into law the Jumpstart Our Business Startups Act (“JOBS Act,” or “the Act”), which represents the most significant relaxation of the initial public offering and public company reporting requirements to be enacted in recent times. The Act provides significant revisions to certain securities laws that affect private companies and to rules relating to access to capital in unregistered offerings. These revisions will likely increase capital flow to start-up companies that previously may have been reluctant to enter the public markets due to regulatory burdens. The Act:

- creates a transitional “on-ramp” for emerging growth companies by reducing the disclosure requirements in their IPO registration statement and reduces compliance and disclosure requirements following the completion of an emerging growth company’s IPO;
- eases prohibitions on general solicitation and general advertising, allowing communication about an offering prior to any filings being made with the SEC;
- raises the threshold at which a private company must report with the SEC, from the current threshold of 500 shareholders of record to either (i) 2,000 shareholders of record or (ii) 500 shareholders of record who are not accredited investors, with higher thresholds for banks and bank holding companies;
- adopts exemptions for certain “crowdfunding” transactions, including preempting state securities laws by making securities offered under exempt offerings “covered securities;” and
- permits companies to conduct offerings to raise up to \$50 million through a process similar to current Regulation A.

## **IPO On-Ramp and Relaxation of Public Reporting Requirements for Emerging Growth Companies**

The JOBS Act significantly eases certain aspects of the initial public offering process for a private company that qualifies as an “Emerging Growth Company,” or “EGC,” and relaxes certain reporting obligations for the post-IPO EGC.

### **Emerging Growth Company Status**

An “emerging growth company” is an issuer that had total annual gross revenues of less than \$1 billion during its most recently completed fiscal year. A company will remain an EGC until (i) it has total annual gross revenues of \$1 billion or more, (ii) the fifth anniversary of its IPO, (iii) it has issued more than \$1 billion in non-convertible debt, or (iv) it has \$700 million of publicly issued stock. An

issuer that sold its common stock in an IPO prior to December 8, 2011 is not eligible to be an emerging growth company.

### Initial Public Offering Process Reforms

The Act provides the following benefits to EGCs:

- **Reduced Financial Statement Requirements** — An EGC will be required to include only two years of audited financial statements in its IPO registration statement (rather than the three years currently required), and the discussion of the company's financial position and results of operations will be limited to the periods disclosed.
- **Confidential Registration Statement Filing** — An EGC will be permitted to submit a draft of its IPO registration statement for confidential review by the SEC staff, provided that the registration statement and all amendments are publicly filed at least 21 days prior to the issuer conducting its road show.
- **Pre-Filing Marketing** — An EGC may "test the waters," or communicate with qualified institutional buyers and institutional accredited investors to gauge investor interest in its securities and offering, either prior to or following the time the EGC files its IPO registration statement.

### Public Company Reporting Reforms

The Act lessens the reporting and compliance burden on an EGC following the completion of its IPO by enacting the following changes:

- **Exemption from auditor attestation of internal controls under Sarbanes-Oxley** — An EGC will not be required to provide an auditor attestation of internal controls. However, (i) the EGC's management will be required to establish, maintain and assess internal controls and (ii) the EGC's CEO and CFO will be required to provide the compliance certifications required under Sarbanes-Oxley.
- **Reduction of Executive Compensation Disclosure** — An EGC will not be required to provide the full range of executive compensation disclosures required of other domestic reporting companies, and instead is permitted to comply with the standards applicable to small business reporting companies.
- **Exemption from Say-on-Pay Vote** — An EGC will not be required to hold the advisory vote on say-on-pay, say on frequency or approval of golden parachute payments until the end of the third year following the EGC's IPO or within one year of having lost its EGC status. In addition, for as long as an issuer is an EGC, it will not have to comply with the disclosures

required under the Dodd-Frank Act with respect to (i) the relationship between executive compensation and the issuer's financial performance, and (ii) the ratio between CEO and median employee compensation.

- **Delays in Compliance with New Accounting Standards** — An EGC will not be required to comply with any new or revised financial accounting standard until the date that such accounting standard becomes applicable to private companies.
- **Exemption from PCAOB Rules regarding Auditor Rotation** — An EGC will not be subject to any of the potential future rules requiring audit firm rotation or a supplement to the auditor's report providing additional information on the company's financial statement audit.

### Research Reports Reforms

The JOBS Act significantly changes current law and rules regarding investment banks and analysts in connection with offerings by EGCs by:

- permitting analysts to publish or distribute research reports about an EGC that proposes to register an offering (or is in registration), even if the party producing the report is participating in the offering (and the research report will not be deemed an "offer" under the Securities Act);
- permitting analysts to participate in meetings with an EGC, even if such meetings include investment banking personnel; and
- permitting broker-dealers to publish or distribute research reports or make public appearances with respect to the securities of an EGC, including any reports during any periods following the completion of an IPO. This effectively eliminates the traditional post-IPO "quiet period" with respect to an EGC IPO.

## Private Capital Reforms

### Easing Prohibition Against General Solicitation and Advertising

The JOBS Act mandates that, within 90 days following enactment of the Act, the SEC revise the private offering exemption under Rule 506 of Regulation D to provide that securities sold in these private offerings may be offered by means of general solicitation or general advertising, provided that all purchasers of the securities are accredited investors. An issuer will be required to take "reasonable steps" to verify that investors are accredited investors, using such methods as determined by the SEC. Likewise, the SEC is required, within 90 days following enactment of the Act, to revise Rule 144A to provide that securities sold under such exemption may be offered by means of general solicitation or

general advertising, provided that securities are sold only to persons the issuer reasonably believes to be qualified institutional buyers (QIBs).

The JOBS Act also creates an exemption from broker-dealer registration requirements for various classes of persons, including those who maintain certain online or other platforms and engage in general advertising or general solicitation, persons who co-invest in the offered securities and persons who provide ancillary services with respect to offered securities.

### **Crowdfunding**

“Crowdfunding” is the collective effort of people who pool their money and other resources together, often via online social networks, to support a common interest. When crowdfunding is used for commercial goals, there is an opportunity for participants to share in the venture’s profits. At this point, federal and state securities laws begin to apply.

The JOBS Act creates a new “crowdfunding exemption” pursuant to which a company will be able to publicly offer and sell, without registration under the Securities Act, securities in “crowdfunding” transactions, subject to the following restrictions:

- The aggregate amount sold to all investors is not more than \$1 million.
- The aggregate amount sold to any investor does not exceed:
  - the greater of \$2,000 or 5% of the annual income or net worth of the investor, (investor income or net worth of less than \$100,000); and
  - 10% of the annual income or net worth of the investor, up to a maximum of \$100,000 (investor net worth of \$100,000 or more).
- The transaction is conducted through a broker or funding portal that complies with the specific intermediary requirements of the new exemption.
- The issuer complies with the specific issuer requirements of the new exemption.

The new crowdfunding exemption is not available to foreign companies, SEC reporting companies and investment companies. Any stock issued in a crowdfunding transaction will be subject to transfer restrictions and may not be transferred during the one-year period beginning on the date of purchase, unless the securities are transferred (i) to the issuer, (ii) to an accredited investor, (iii) as part of an offering registered with the SEC, or (iv) to a member of the family of the purchaser.

### **Amendments to Regulation A**

The JOBS Act requires the SEC to increase the aggregate offering amount of securities sold within any 12-month period under the Regulation A exemption from \$5 million to \$50 million. The securities sold pursuant to the exemption may be offered and sold publicly, and such securities will not be restricted securities. An issuer may “test the waters,” or solicit interest in its offering prior to filing any offering statement with the SEC, provided such communications comply with established SEC rules.

The Act requires the SEC to adopt rules requiring that issuers taking advantage of this exemption file audited financial statements annually with the SEC. In addition, the SEC may impose other terms, conditions or requirements that it determines necessary for investor protection, including a requirement that the issuer prepare and file electronically with the SEC and distribute to prospective investors an offering statement and any related documents.

### **Raising Exchange Act Registration Thresholds**

The JOBS Act increases the number of shareholders of record that a non-reporting company may have before it is required to register under the Exchange Act to either (i) 2,000 shareholders or (ii) 500 shareholders who are not accredited investors. The current \$10 million asset test has not been revised by the new amendments. In addition, the SEC must establish rules that exclude securities sold in exempt “crowdfunding” offerings from the determination of holders of record.

The Act also provides that, in the case of an issuer that is a bank or a bank holding company, that entity must register under the Exchange Act no later than 120 days after the last day of its first fiscal year on which the issuer has total assets exceeding \$10 million and a class of equity security (other than an exempted security) held of record by 2,000 or more persons, without further limiting the number of shareholders that are not accredited investors. In the case of a bank or a bank holding company, the issuer will no longer be subject to reporting if the number of holders falls below 1,200 persons.

### **Conclusion**

The new IPO on-ramp provisions of Title I of the JOBS Act should make launching an IPO a more appealing option to a company than it has been in the past. Most notably, we see companies benefiting from the potential costs savings that may be derived from the more limited financial disclosures required by the JOBS Act, and we believe that companies will take advantage of the ability to conduct meetings with institutional accredited investors and qualified institutional buyers before launching an offering. In addition, companies that qualify as emerging growth companies will benefit from the eased reporting and compliance requirements.

The JOBS Act's private offering provisions have the potential to have an even broader impact on when and how companies access capital markets because, in many cases, they apply to all companies, not only non-reporting companies. The increase in the reporting thresholds in the JOBS Act will have an immediate effect on companies currently faced with the decision of whether to go public. Although the JOBS Act's effect still depends on upcoming SEC rulemaking, the Act will, at least to some degree, ease the path to capital for many companies, both public and private.

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