

New SEC Proposed Amendments Seek to Improve and Harmonize Private Offering Exemptions

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On March 4, 2020, the Securities and Exchange Commission (the “Commission”) proposed amendments to the private offering exemptive framework under the Securities Act of 1933, as amended (the “Securities Act”) to “simplify, harmonize, and improve certain aspects of the framework” with the goal of promoting capital formation while maintaining investor protections.

The current private offering framework is a set of exemptions and safe harbors which permit issuers to raise capital through various, differing rules which don’t require the filing of a registration statement with the Commission under the Securities Act. These rules are meant to provide issuers with a less expensive and more efficient alternative to a registered public offering in exchange for certain limitations and requirements being placed on the offering, typically regarding the number and type of investors, the type and context of solicitations, the size of the offering and individual investments and certain limited information requirements.

The conflicting requirements of the current, differing rules and the potential integration (determination of whether multiple transactions are part of the same offering) of offerings conducted under this “patchwork system” has resulted in a complex and sometimes confusing regulatory framework where the interaction of offerings conducted under the various exemptions and safe harbors is often uncertain, leading to potential violations of the Securities Act. As Chairman Clayton stated in relation to the proposed amendments, “[t]he complexity of the current framework is confusing for many involved in the process, particularly for those smaller companies whose limited resources spent on navigating our overly complex rules are diverted from direct investments in the companies’ growth.”

As noted in the Commission’s press release, “[t]he Commission’s proposed amendments are intended to reduce potential friction points to make the capital raising process more effective and efficient to meet evolving market needs.” The proposed amendments would:

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- address, in one broadly applicable rule, the ability of issuers to move from one exemption to another, and ultimately to a registered offering;
- increase the offering limits for Regulation A, Regulation Crowdfunding, and Rule 504 offerings, and revise certain individual investment limits;
- provide greater certainty to issuers and protection to investors by setting clear and consistent rules governing offering communications between investors and issuers, including permitting certain “demo day” activity without running afoul of the prohibition on general solicitation; and
- harmonize certain disclosure and eligibility requirements and bad actor disqualification provisions to reduce differences between exemptions.

The proposed amendments reflect comments received in response to the Commission’s concept release issued in June of 2019. The comment period for the proposed amendments will remain open for 60 days following publication in the Federal Register. The full proposal is available [here](#).

Integration Framework

The current integration framework for registered and exempt offerings under the Securities Act consists of a mixture of rules and Commission staff guidance for determining whether multiple securities transactions should be considered part of the same offering.

The proposed amendments set forth a “general principle of integration that looks to the particular facts and circumstances of the offering, and focuses the analysis on whether the issuer can establish that each offering either complies with the registration requirements of the Securities Act, or that an exemption from registration is available for the particular offering.”

The amendments also detail four non-exclusive safe harbors from integration, as set forth in this table from the Commission’s press release:

Safe Harbor 1	Any offering made more than 30 calendar days before the commencement of any other offering, or more than 30 calendar days after the termination or completion of any other offering, would not be integrated with another offering; provided that, for an exempt offering for which general solicitation is not permitted, the purchasers either were not solicited through the use of general solicitation, or established a substantive relationship with the issuer prior to the commencement of the offering for which general solicitation is not permitted.
Safe Harbor 2	Offers and sales made in compliance with

	Rule 701, pursuant to an employee benefit plan, or in compliance with Regulation S would not be integrated with other offerings.
Safe Harbor 3	An offering for which a Securities Act registration statement has been filed would not be integrated with another offering if made subsequent to: (i) a terminated or completed offering for which general solicitation is not permitted; (ii) a terminated or completed offering for which general solicitation is permitted and made only to qualified institutional buyers and institutional accredited investors; or (iii) an offering that terminated or completed more than 30 calendar days prior to the commencement of the registered offering.
Safe Harbor 4	Offers and sales made in reliance on an exemption for which general solicitation is permitted would not be integrated with another offering if made subsequent to any prior terminated or completed offering.

Offering and Investment Limits

The Commission proposed amendments to the current offering and investment limits for Regulation A, Regulation Crowdfunding and Rule 504 offerings as follows:

For Regulation A

- raise the maximum offering amount under Tier 2 of Regulation A from \$50 million to \$75 million
- raise the maximum offering amount for secondary sales under Tier 2 of Regulation A from \$15 million to \$22.5 million

For Regulation Crowdfunding

- raise the offering limit in Regulation Crowdfunding from \$1.07 million to \$5 million
- amend the investment limits for investors in Regulation Crowdfunding offerings by:
 - not applying any investment limits to accredited investors
 - revising the calculation method for investment limits for non-accredited investors to allow them to rely on the greater of their annual income or net worth when calculating the limit on how much they can invest

For Rule 504 of Regulation D

- raise the maximum offering amount from \$5 million to \$10 million

Regulation A and Regulation Crowdfunding Eligibility

Currently, specific eligibility restrictions excluding certain types of entities or activities by issuers apply to both Regulation A and Regulation Crowdfunding, respectively. While Regulation Crowdfunding does not restrict the types of securities eligible to be sold under the exemption, the types of securities eligible for sale under Regulation A are limited to equity securities, debt securities, and securities convertible or exchangeable to equity interests, including any guarantees of such securities. Regulation Crowdfunding excludes the use of special purpose vehicles and Regulation A excludes issuers that have not filed required reports under Regulation A in the two prior years.

The proposed amendments would harmonize Regulation A and Regulation Crowdfunding by restricting Regulation Crowdfunding to the same eligible securities as Regulation A. The proposed rules would also amend Regulation Crowdfunding to permit the use of certain special purpose vehicles and amend Regulation A to expand its exclusion of issuers to also include issuers that have not filed required reports under Section 13 or 15(d) of the Securities Exchange Act of 1934, as amended (the “Exchange Act”).

“Test-the-Waters” Communications

The Commission proposed several amendments relating to offering communications.

Proposed new Rule 241 that would permit an issuer to use generic solicitation of interest materials to “test-the-waters” for an exempt offer of securities prior to determining which exemption it will use for the sale of the securities. As proposed, Rule 241(b) would require the materials used under this exemption to bear a legend or disclaimer notifying potential investors that (1) the issuer is considering an offering of securities exempt from registration under the Securities Act, but has not determined a specific exemption from registration the issuer intends to rely upon for the subsequent offer and sale of the securities; (2) no money or other consideration is being solicited, and if sent, will not be accepted; (3) no sales will be made or commitments to purchase accepted until the issuer determines the exemption under which the offering is intended to be conducted and, where the exemption includes filing, disclosure, or qualification requirements, all such requirements are met; and (4) a prospective purchaser’s indication of interest is non-binding.

The Commission also proposed a rule amendment that would permit Regulation Crowdfunding issuers to “test-the-waters” prior to filing an offering document with the Commission in a manner similar to current Regulation A.

“Demo Day” Communications

A proposed new Rule 148 that would provide that certain “demo day” communications would not be deemed general solicitation or general advertising. Specifically, as proposed, an issuer would not be deemed to have engaged in general solicitation if the communications are made in connection with a seminar or meeting by a college, university, or other institution of higher education, a local government, a nonprofit organization, or an angel investor group, incubator, or accelerator sponsoring the seminar or meeting.

With respect to the organization and conduct of the event, the sponsor would not be permitted to make investment recommendations or provide investment advice to attendees of the event, nor would it be permitted to engage in any investment negotiations between the issuer and investors attending the event. The sponsor would not be permitted to charge attendees of the event any fees, other than reasonable administrative fees, or receive any compensation for making introductions between attendees and issuers, or for investment negotiations between the parties. The sponsor also would not be permitted to receive any compensation with respect to the event that would require it to register as broker or dealer under the Exchange Act, or as an investment adviser under the Advisers Act.

In addition, the proposed Rule 148 would specify that the advertising for the event may not reference any specific offering of securities by the issuer and that the information conveyed at the event regarding the offering of securities by the issuer is limited to:

- Notification that the issuer is in the process of offering or planning to offer securities;
- The type and amount of securities being offered; and
- The intended use of the proceeds of the offering.

Other Improvements to Specific Exemptions

The proposed amendments would also:

- change the financial information that must be provided to non-accredited investors in Rule 506(b) private placements to align with the financial information that issuers must provide to investors in Regulation A offerings- specifically, for Regulation D offerings of up to \$20 million in securities, issuers would no longer be required to provide audited financial statements and would instead be required to comply with the requirements which apply to Tier 1 Regulation A offerings and for Regulation D offerings of greater than \$20 million in securities, issuers would be required to provide audited financial statements and comply with requirements similar to Tier 2 Regulation A offerings;
- add a new item to the non-exclusive list of verification methods in Rule 506(c) that would allow an issuer to establish that an investor for which the issuer previously took reasonable steps to verify as an accredited investor remains an accredited investor as of the time of a subsequent sale if the investor provides a written representation to that effect and the issuer is not aware of information to the contrary;
- simplify certain requirements for Regulation A offerings and establish greater consistency between Regulation A and registered offerings; and

- harmonize the bad actor disqualification provisions in Regulation D, Regulation A, and Regulation Crowdfunding by adjusting the look-back requirements in Regulation A and Regulation Crowdfunding to also refer to the time of sale (as opposed to only referencing the time the issuer files an offering statement).