

# Morgan Lewis

**GLOBAL PUBLIC COMPANY ACADEMY**

## **REGULATION A+ OFFERINGS AND RELATED DEVELOPMENTS**

**Albert Lung**  
**Emily Drazan Chapman**

May 1, 2019



# Regulation A+

- June 2015 – Substantially amended and revised the then existing Regulation A, which was not used due to the low dollar threshold (\$5 million).
- Provides for U.S. and Canadian companies to raise up to \$50 million in a public offering by filing and qualifying an offering statement with the SEC.
  - A simplified and abbreviated process of registration
  - Accelerated SEC review process with reduced disclosures compared to registration statement.
- The SEC recently changed rules to allow public companies to rely on Regulation A+.

# Regulation A+ Basics

- Two Tiers of Offering:
  - Tier 1 offering: up to \$20 million in 12 month period
  - Tier 2 offering: up to \$50 million in 12 month period
  - Tier 2+ for NASDAQ listed transaction: additional disclosures and PCAOB audit—mini-IPO.
- Major distinctions between Tier 1 and Tier 2:
  - Audited Financial Statements
  - Federal preemption/State Blue Sky Review
  - Investment Limitation
  - On-going reporting requirements (annual report and semi-annual report)
  - Disclosure requirements
- Regulation A+ Process: Similar to registered process but simpler and faster
- A convenient tool to offer securities for social media and consumer based companies.

## Treatment under Section 12(g)

- Regulation A conditionally exempts securities issued in a Tier 2 offering from the mandatory registration provisions of Section 12(g) for so long as the issuer remains subject to, and is current in (as of its fiscal year end), its Regulation A periodic reporting obligations and had a public float of less than \$75 million or less than \$50 million in annual revenue if there is no public float.
- An issuer that exceeds the size-based requirements is granted a two-year transition period before it would be required to register its class of securities pursuant to Section 12(g), provided it timely files all ongoing reports due during such period.
- Additionally, in order for the conditional exemption to apply, issuers in Tier 2 offerings are required to engage the services of a transfer agent registered with the Commission pursuant to Section 17A of the Exchange Act.

# Regulation A+: Test the Water

- Rule 255 provide an innovation in general solicitation: testing the water communications, which materially modified the “gun jumping” prohibition.
  - A company may “communicate orally or in writing to determine whether there is any interest in a contemplated securities offering . . . . No solicitation or acceptance of money or other consideration, nor of any commitment, binding or otherwise, from any person is permitted until qualification of the offering statement”
- Provides an opportunity for companies to assess the interest of investors and obtain a better understanding of the market for the securities.
- TTW can be done at anytime prior to or after the filing of Offering Statement on Form 1-A.
- Unlike the EGC IPO rules, TTW is extended to include non-accredited investors, thus it is designed for website general solicitation.

# Regulation A+ Rule 255 Requirements

- Filing of TTW materials with the Form 1-A; subject to SEC review.
- No requirement to file TTW materials immediately prior to or after its use at the meeting—the filing would occur only in connection with the next filing of the Form 1-A.
- No filing of substantially same materials.
- Companies cannot take or accept any orders from investor.
- All written materials must contain the Rule 255 legend—a disclaimer to confirm that no money can be accepted until the Form 1-A is qualified.
- Links to preliminary offering circular if available.
- Subject to anti-fraud provisions of Securities Act.

# Website and Online Offering: Regulation A+

- Popularity of Regulation A+ created a cottage industry of funding portals and crowdfunding websites has, such as SeedInvest, StartEngine and others.
- Broker dealer registration requirements may be implicated.
- Advantages:
  - No verification of accredited investor status.
  - No prohibition on the pool of investors.
- Disadvantages:
  - Cost of preparing Form 1-A
  - No state law preemption.
- Best practices: (i) Review content of TTW materials; (ii) avoid financial projections; (iii) returning materials to the company.

# Investment Limitations in Tier 2 Offerings

- Regulation A limits the amount of securities that an investor who is not an “accredited investor” under Rule 501(a) of Regulation D can purchase in a Tier 2 offering to no more than:
  - 10% of the greater of annual income or net worth (for natural persons); or
  - 10% of the greater of annual revenue or net assets at fiscal year-end (for non-natural persons).
- This limit does not apply to purchases of securities that will be listed on a national securities exchange upon qualification.

# Secondary Trading Considerations

- **Post-offering liquidity and secondary trading market is a key consideration.**
- **OTC Market versus Nasdaq/NYSE**
  - Regulation A does not provide preemption for secondary trading. Unlike NASDAQ, OTC securities are not “covered securities” and companies must apply for manual exemptions.
  - NASDAQ and OTC listing requirements
- **OTC Market:** Three primary tiers: (1) OTCQX; (2) OTCQB; (3) OTCPIK
  - Qualification standards such as minimum bid price, market cap and other financial and liquidity criteria.
  - Financial Reporting: Regulation A+ Reporting is sufficient for OTCQB, but OTCQX requires additional quarterly reports: Rule 144 and Rule 15c2-11 considerations.
  - OTCQX requires PCAOB registered auditors (although not PCAOB audit standard)
- **Nadaq Listing:**
  - Additional disclosures in the Form 1-A, except for financial statements.
  - Listing Qualifications: Public float requirement
  - PCAOB Audit
  - Form 8-A: Must be filed with 5 days of qualification of Form 1-A

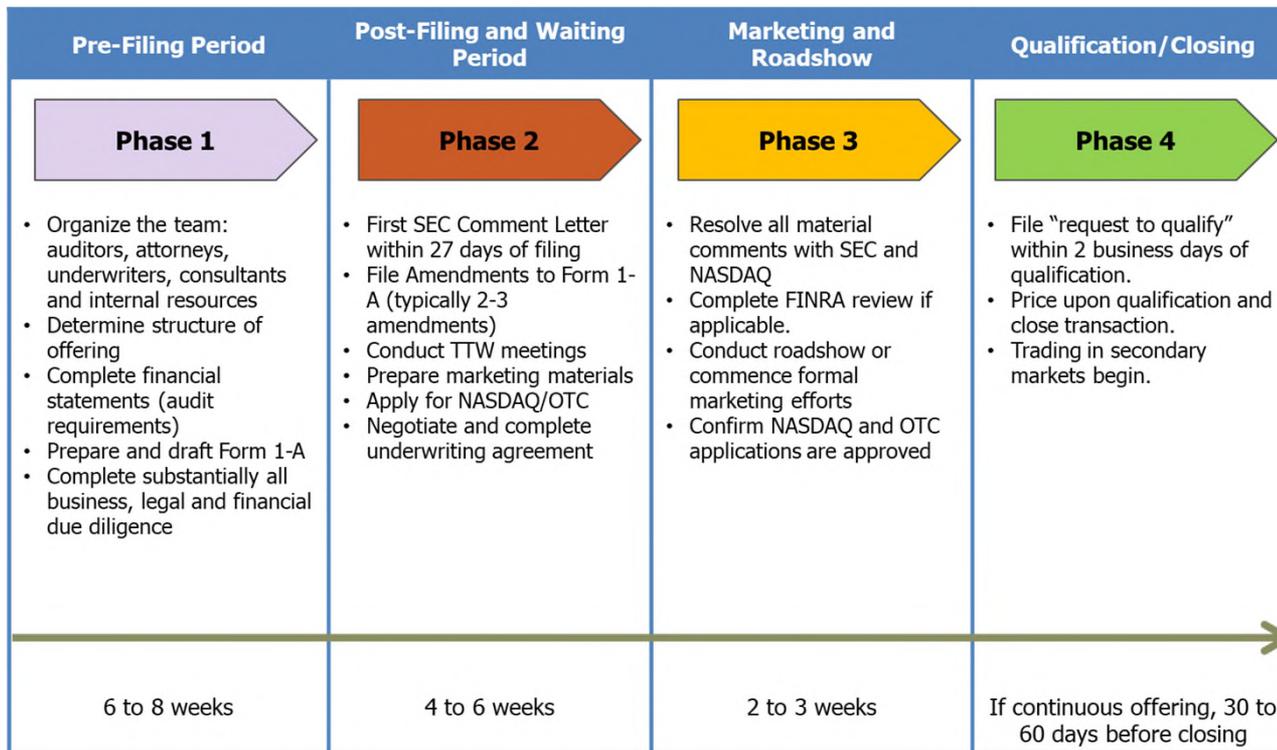
# Regulation A+ Marketing Strategies

- Combination of Testing the Water Communications (TTW) and formal roadshows.
  - Consumer/Customer based offering—marketing to existing customers as potential investor, particularly internet companies.
- Regulation A+ TTW provides more flexibility to TTW under Title I IPO on ramp: Not restricted to QIB and institutional accredited investors.
- Unlike TTW under Title I, all Regulation A+ TTW materials must be filed with the SEC “as an exhibit” to the Form 1-A.
  - TTW encompasses a large categories of materials.
  - Review content for consistency and accuracy.
  - No need to file multiple slide decks if they are substantively the same as materials previously filed.
  - SEC is focused on reviewing TTW materials
  - Best practices: forward looking statement; written script; no broad distribution of materials at investor meetings.
- Distinctions between TTW and roadshow—unclear but may be relevant in terms of disclosures.

# Marketing Must Change After Qualification

- Once an offering is qualified a prospectus must precede or accompany any offer.
  - This means that there can be no print or television ads once qualified.

# Regulation A+ IPO Timeline (Tier 2 Offering) (4 to 5 months)



# Form 1-A: Process and Disclosure Issues

- Form 1-A generally follows the traditional S-1 process:
  - No filing fees are required
  - SEC review process is streamlined;
  - Response letter filed on EDGAR
  - More flexibility in the review process with SEC examiner; and
- Financial Statement requirements
  - Instead of the 135-day stale period, Form 1-A provide a 9-month period.
- Ability to use to use “Offering Circular Supplement” for omission of pricing and other information under Rule 430A prior to qualification
  - 20% Safe harbor for upsizing and downsizing transaction without recirculation.
  - Cannot change the number of shares disclosed in the offering statement

# Part I of Form 1-A

- Notice Document
  - Item 1. (Issuer Information) requires information about the issuer’s identity, industry, number of employees, financial statements and capital structure, as well as contact information.
  - Item 2. (Issuer Eligibility) requires the issuer to certify that it meets various issuer eligibility criteria.
  - Item 3. (Application of Rule 262 (“bad actor” disqualification and disclosure)) requires the issuer to certify that no disqualifying events have occurred and to indicate whether related disclosure will be included in the offering circular.
  - Item 4. (Summary Information Regarding the Offering and other Current or Proposed Offerings) includes indicator boxes or buttons and text boxes eliciting information about the offering.
  - Item 5. (Jurisdictions in Which Securities are to be Offered) requires information about the jurisdiction(s) in which the securities will be offered.
  - Item 6. (Unregistered Securities Issued or Sold Within One Year) requires disclosure about unregistered issuances or sales of securities within the last year.

# “Bad Actor” Disqualification

- Regulation A is unavailable for “bad actors.”
  - “Bad Actors” are “Covered Persons” who are subject to “Disqualifying Events.”
- Examples of “Covered Persons”:
  - Issuer and any predecessor or affiliate issuer
  - Director or executive officer
  - Any placement agent or compensated solicitor
- Examples of “Disqualifying Events”:
  - Criminal convictions related to sale of security of false filing with SEC in last 10 years
  - SEC disciplinary orders related to SEC regulated persons
  - Suspension by FINRA or an exchange
- “Reasonable Care” exception:
  - Applicable if issuer can prove that it did not know, and could not have reasonably known, of “Bad Actor” status

## Part II of Form 1-A

- Offering Circular - Narrative Disclosure
  - Simplified and scaled version of the narrative disclosure requirements otherwise required to be provided by issuers in registered offerings on Form S-1.
  - In addition to the availability of certain scaled disclosure items, the Offering Circular format was designed to simplify the process by which an issuer prepares its narrative disclosure by limiting the need for issuers to look outside the form for disclosure guidance.

## Part III of Form 1-A

- Issuers are required to file the following exhibits with the offering statement:
  - Underwriting agreement;
  - Charter and by-laws;
  - Instrument defining the rights of securityholders;
  - Subscription agreement;
  - Voting trust agreement;
  - Material contracts;
  - Plan of acquisition, reorganization, arrangement, liquidation, or succession;
  - Escrow agreements; consents; opinion regarding legality; “testing the waters” materials; appointment of agent for service of process; materials related to non-public submissions; and any additional exhibits the issuer may wish to file.

# Reporting Obligations Tier 1

- Issuers in Tier 1 offerings are required to electronically file with the Commission on EDGAR certain summary information on terminated or completed Regulation A offerings in an exit report on Part I of Form 1-Z not later than 30 calendar days after termination or completion of an offering.

# Reporting Obligations Tier 2

- Annual Report
  - Issuers in Tier 2 offerings are required to electronically file annual reports with the Commission on EDGAR on Form 1-K within 120 calendar days of the issuer's fiscal year end.
- Semiannual Report
  - Issuers in Tier 2 offerings are required to electronically file semiannual reports with the Commission on EDGAR on Form 1-SA within 90 calendar days after the end of the first six months of the issuer's fiscal year.

# Reporting Obligations Tier 2

- Current Reports
  - Issuers in Tier 2 offerings are required to electronically file current reports with the Commission on EDGAR on Form 1-U within four business days of the occurrence of one (or more) of the following events:
    - Fundamental changes;
    - Bankruptcy or receivership;
    - Material modification to the rights of securityholders;
    - Changes in the issuer's certifying accountant;
    - Non-reliance on previous financial statements or a related audit report or completed interim review;
    - Changes in control of the issuer;
    - Departure of the principal executive officer, principal financial officer, or principal accounting officer; and
    - Unregistered sales of 10% or more of outstanding equity securities.

## Exit Report Tier 2

- Issuers in Tier 2 offerings that have filed all ongoing reports required by Regulation A 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 Form 1-Z.
- Upon filing a Form 1-Z an issuer may immediately suspend their ongoing reporting obligations under Regulation A at any time after completing reporting for the fiscal year in which the offering statement was qualified, if the securities of each class to which the offering statement relates are held of record by fewer than 300 persons and offers or sales made in reliance on a qualified Tier 2 offering statement are not ongoing.
- In such circumstances, an issuer's obligation to continue to file ongoing reports in a Tier 2 offering under Regulation A would be suspended immediately upon the electronic filing of a notice with the Commission on Part II of Form 1-Z.

# Legal Liabilities to Officer and Directors

- There are two basic provisions under federal securities laws that are implicated by a Regulation A+ Offering:
  - Section 17: Antifraud provision typically reserved for SEC enforcement action.
  - No Section 11 liability but Section 12(a)(2) liability: Strict liability for materially misleading information in Form 1-A
  - no need to allege or prove intent or scienter or reliance
  - No need to prove direct causation that sales would not have occurred if plaintiff knew the statement
  - The mis-statements include both Form 1-A and any oral communications
  - Officers, directors and controlled persons are liable.
- State law: fiduciary duty issues.
- Due diligence defense for underwriters.
- Practical considerations

# Q&A

QUESTION

ANSWER

# CLE

- If you registered noting that you need CLE the code is **EFDR695**. Please be sure fill out the post event survey and enter this code and save this number; you will need this to receive a Certificate of Attendance. You will be contacted within 30-60 days by our CLE administrative team.
- We will process your credits for other states where this program has been approved.
- Questions? Please email Aisha Khan at [Aisha.khan@morganlewis.com](mailto:Aisha.khan@morganlewis.com)

# Albert Lung



**Of Counsel**  
**Morgan Lewis**  
[albert.lung@morganlewis.com](mailto:albert.lung@morganlewis.com)  
+1.650.843.7263

Albert Lung advises companies throughout the United States and abroad on capital market transactions, corporate governance, and securities laws. His clients include publicly listed companies and investment banking firms in emerging technology, biotechnology, software, and life sciences fields. Albert advises clients in public and private offerings, compliance with US Securities and Exchange Commission (SEC) regulations and disclosure requirements, NASDAQ/NYSE listing requirements, corporate governance, investors communications, and a variety of other general corporate matters.

# Emily Drazan Chapman



**Associate**  
**Morgan Lewis**

[emily.chapman@morganlewis.com](mailto:emily.chapman@morganlewis.com)

+1.202.739.5699

Emily Drazan Chapman counsels companies with respect to the federal securities laws, corporate governance matters, and responding to activist shareholder campaigns. Prior to joining Morgan Lewis, Emily was an attorney-adviser with the US Securities and Exchange Commission (SEC) in the Division of Corporation Finance where she reviewed transactional filings under the Securities Act of 1933 and periodic reports and proxy statements under the Securities Exchange Act of 1934.

Emily also served in the SEC's Division of Corporation Finance's Office of Small Business Policy, where she provided interpretative guidance on exemptions to SEC registration and reviewed applications for bad actor waivers.

## Our Global Reach

Africa  
Asia Pacific  
Europe  
Latin America  
Middle East  
North America

## Our Locations

Almaty	Chicago	Houston	Orange County	Shanghai*
Astana	Dallas	London	Paris	Silicon Valley
Beijing*	Dubai	Los Angeles	Philadelphia	Singapore
Boston	Frankfurt	Miami	Pittsburgh	Tokyo
Brussels	Hartford	Moscow	Princeton	Washington, DC
Century City	Hong Kong*	New York	San Francisco	Wilmington



# Morgan Lewis

\*Our Beijing and Shanghai offices operate as representative offices of Morgan, Lewis & Bockius LLP. In Hong Kong, Morgan Lewis operates through Morgan, Lewis & Bockius, which is a separate Hong Kong general partnership registered with The Law Society of Hong Kong as a registered foreign law firm operating in Association with Luk & Partners. Morgan Lewis Stamford LLC is a Singapore law corporation affiliated with Morgan, Lewis & Bockius LLP.

# THANK YOU

© 2019 Morgan, Lewis & Bockius LLP  
© 2019 Morgan Lewis Stamford LLC  
© 2019 Morgan, Lewis & Bockius UK LLP

Morgan, Lewis & Bockius UK LLP is a limited liability partnership registered in England and Wales under number OC378797 and is a law firm authorised and regulated by the Solicitors Regulation Authority. The SRA authorisation number is 615176.

Our Beijing and Shanghai offices operate as representative offices of Morgan, Lewis & Bockius LLP. In Hong Kong, Morgan Lewis operates through Morgan, Lewis & Bockius, which is a separate Hong Kong general partnership registered with The Law Society of Hong Kong as a registered foreign law firm operating in Association with Luk & Partners. Morgan Lewis Stamford LLC is a Singapore law corporation affiliated with Morgan, Lewis & Bockius LLP.

This material is provided for your convenience and does not constitute legal advice or create an attorney-client relationship. Prior results do not guarantee similar outcomes. Attorney Advertising.