

Implementation of JOBS Act provisions a long way off

Commentary by Timothy M. Sullivan and Eliot C. Abbott

The JOBS Act was signed by President Barack Obama on April 5. One of the goals of the legislation was to allow companies easier access to capital, thereby allowing them to expand their businesses and hire new workers.



Sullivan

The act provides that emerging growth companies will be exempt from certain Security and Exchange Commission requirements for up to five years, expands the number of shareholders a company may have before becoming subject to various SEC rules, authorizes companies to advertise when conducting certain private placements, permits a company to sell up to \$50 million of securities under relaxed registration rules (IPO lite) and allows for crowd-funding.



Abbott

Three of these provisions — advertising in private placements, crowd-funding and IPO lite — will not be effective until the SEC adopts rules implementing them. As of this writing, none of rules has been adopted and the likelihood of their adoption in the near term is doubtful, thus thwarting one of the JOBS Act's purposes.

The advertising provision would permit companies selling securities under Rule 506 of Regulation D to advertise their offerings as long as sales are only made to accredited investors — an investor with a net worth of \$1 million or more (exclusive of the value of the investor's principal residence) or who has made \$200,000 (or \$300,000 with his spouse) in 2011, 2012 and expects to do



GERRY BROOME/AP

Three of the provisions of President Barack Obama's JOBS Act will not be effective until the SEC adopts rules implementing them, and the likelihood of their adoption in the near term is doubtful, write Timothy M. Sullivan and Eliot C. Abbott of Hinshaw & Culbertson.

so in 2013.

This rule change will allow companies seeking to raise capital access to a wider audience of investors. An examination of the Rule 506 filings for 2011 indicated that companies anticipated selling \$895 billion of securities under this rule.

The SEC proposed rules to eliminate the advertising ban in August 2012. These rules have not been finalized. Currently, the SEC is deadlocked, with two Republican and two Democratic commissioners. Mary Schapiro resigned as SEC chairman in December, and the president has indicated that he intends to appoint Mary Jo White to serve as chairman.

Presently, it is anticipated that these rules will not be finalized until a new SEC chairman has been appointed and approved by the U.S. Senate. As this process may take a while, the final advertising rules will not be in place for some time but, hopefully, by the end of the

summer.

Crowd-funding allows a company to use the Internet to raise small amounts of capital — up to \$1 million in any 12-month period — from a large group of investors who will be permitted to invest small amounts in each offering. In theory, the provision will allow investors to make small investments in a start-up while keeping the start-up's capital raising costs low.

The SEC has not proposed rules on crowd-funding even though the JOBS Act directed the agency to adopt rules by Dec. 31. There is a tension between those who view the crowd-funding provision as an excellent opportunity to assist smaller companies in raising capital and those concerned that the easing of the capital raising rules will strip investors of important protections — possibly creating mini-Madoff schemes. It is anticipated that rules proposed by the SEC will be carefully scrutinized by both of these groups.

Additionally, the SEC is substantially behind in adopting rules required under the

Dodd-Frank Wall Street Reform and Consumer Protection Act. The SEC rules backlog, when coupled with the deadlock among the SEC commissioners and the probable extended period needed for the rulemaking process in light of the conflicting concerns, means that it is unlikely that crowd-funding rules will be in place before the end of 2013.

Presently, crowd-funding as defined in the JOBS Act is illegal. Several websites, however, offer a version of crowd-funding that is becoming quite popular. These websites investigate start-ups and, if satisfied with the quality of the company, allow investors, who have been pre-screened to insure compliance with securities law sophistication requirements, to invest in these companies. The websites provide a variety of information about the start-ups such as financials and projections. Many persons who would invest in a company under the SEC crowd-funding rules would not be able to meet the investor sophistication requirements imposed by these websites.

Companies using the IPO-lite provisions will be able to sell up to \$50 million of stock publicly, without having to register with the SEC. Additionally, the shares may be publicly resold and are not subject to state securities laws.

The JOBS Act IPO-lite provisions do not direct the SEC to adopt the required rules by a specified date. However, the legislation does instruct the agency to review the \$50 million limit within two years of passage of the JOBS Act, creating the logical conclusion that Congress anticipated that the SEC would adopt rules by April 5, 2014. In light of the deadlock at the SEC and the backlog, it is not likely that these provisions will be implemented before 2014.

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