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Regulation A Availability for Securities Offerings by Smaller Reporting Companies

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What You Need To Know:

- **Regulation A is being made available to all reporting companies.**
- **The change will likely have the greatest benefit for smaller reporting companies.**
- **The availability of Regulation A will make it easier for smaller reporting companies to raise capital as compared to current options.**

On May 24, 2018, the Economic Growth, Regulatory Relief, and Consumer Protection Act was signed into law. While press coverage of the Act mostly focused on its rollback of regulations applicable to financial institutions and originating in the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, significantly, the new Act also requires the U.S. Securities and Exchange Commission (SEC) to amend its rules to permit reporting companies to use Regulation A.

Regulation A provides an exemption from the registration provisions of the Securities Act of 1933, as amended (Securities Act), by permitting offerings of up to $20 million in any one-year period (Tier 1 Offerings) and offerings of up to $50 million in any one-year period (Tier 2 Offerings) subject to compliance with certain requirements. Until now, Regulation A has only been available to U.S. and Canadian issuers that were not subject to the reporting requirements of the Securities Exchange Act of 1934, as amended (Exchange Act). However, the new law orders the SEC to remove this eligibility requirement, making Regulation A available to all reporting companies, and mandates that the ongoing reporting obligations associated with Tier 2 Offerings are satisfied by Exchange Act reporting (which a public company already does).

What This May Mean for Smaller Public Companies

There are three significant advantages that this expansion of Regulation A is expected to have for smaller companies that are already public.

First, reporting companies that do not trade on national securities exchanges (for example, those that trade in the over-the-counter markets) will be able to avoid state securities law requirements by conducting future offerings in compliance with Tier 2 of Regulation A.

Second, Regulation A permits issuers to do significant investor outreach prior to submitting an offering statement to the SEC, including solicitations of written indications of interest. That outreach will enable smaller reporting companies to gauge investor interest in their securities by contacting retail as well as institutional investors before committing to the expense of preparing an offering circular.

Third, Regulation A will allow smaller public companies to make offerings to retail investors through a general solicitation without having to comply with the burdensome income verification requirements of Rule 506(c) under Regulation D.

Offerings Off-the-Shelf

Rule 251(d)(3) of Regulation A permits certain offerings to be made on a delayed or continuous basis pursuant to a qualified offering statement. However, as currently written, Rule 251(d)(3) would not permit an issuer to conduct a delayed primary offering "off-the-shelf." In the spirit of the legislation, the SEC may decide to expand Rule 251(d)(3) to permit shelf offerings to expand the utility of Regulation A and bring it into closer conformity with Rule 415. However, if the SEC elects to do so, it may impose restrictions on such offerings, including limitations on which issuers can use any shelf offering procedure and limitations on the amount that may be sold, similar to those contained in the "baby shelf" rule in General Instruction I.B.6. to Form S-3.

Eligibility

Regulation A is not available to certain issuers, such as companies organized outside the U.S. and Canada; shell companies; investment companies; issuers of interests in oil, gas and other mineral rights; issuers of asset-backed securities; issuers that have had their securities denied or suspended from registration by the SEC within the past five years; and issuers that are disqualified by any "bad actor" events involving the issuer or any of its affiliates. However, this expansion of Regulation A is likely to provide significant relief to qualifying smaller reporting companies.

The full text of S.2155, Economic Growth, Regulatory Relief, and Consumer Protection Act is available here.

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