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## JOBS Act: Focus on Foreign Private Issuers

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**The enactment of the US JOBS Act will relax certain of the requirements and restrictions around securities offerings and public reporting obligations in the United States. These changes will apply to both US domestic and foreign private issuers. The most significant modifications provided by the JOBS Act for foreign issuers accessing the US capital markets include immediately effective changes to the offering process for SEC-registered IPOs and ongoing SEC reporting obligations for companies with less than US\$1 billion in gross revenues, including an exemption for up to five years from the SOX Section 404 requirement to obtain an annual attestation report from a registered public accounting firm; and enhanced publicity for Rule 144A offerings and the facilitation of public offerings of US\$50 million or less to be implemented by SEC rulemaking.**

On April 5, 2012, President Obama signed into law the Jumpstart Our Business Startups Act, also known as the JOBS Act.<sup>1</sup> The JOBS Act has broad implications for many companies, including foreign private issuers, seeking to access the US capital markets, as it reduces some of the regulatory burdens of capital raising and ongoing SEC reporting. The JOBS Act also includes provisions permitting crowdfunding—up to US\$1 million in any 12 months—subject to SEC rulemaking, but that flexibility is limited to US domestic issuers.

### Changes to the US IPO Process for Emerging Growth Companies

The JOBS Act creates a new class of issuer called emerging growth companies, or EGCs, which are defined as companies, whether US domestic or foreign private issuers, that have annual gross revenues of less than US\$1 billion. The vast majority of companies that have recently conducted IPOs in the United States would have fit that definition. Under the JOBS Act, EGCs benefit from a significant relaxation of several restrictions relating to the securities offering process and, in particular, to IPOs, which, for the purposes of the JOBS Act, means the first offering of equity securities registered

<sup>1</sup> The Act, in the form signed by President Obama on April 5, 2012, is available at: <http://www.gpo.gov/fdsys/pkg/BILLS-112hr3606enr/pdf/BILLS-112hr3606enr.pdf>.

with the SEC under the Securities Act.<sup>2</sup> The most significant changes to the IPO and securities offering processes include:

- **Communications Prior to and During a Securities Offering:** EGCs and their authorized representatives, such as underwriters, are permitted to test the waters with qualified institutional buyers (QIBs) and institutional accredited investors (IAIs) to gauge their interest prior to (and after) filing a registration statement for an IPO or any other securities offering. Both oral and written testing-the-waters communications are permitted without triggering the existing “gun-jumping” restrictions on pre-filing communications.

Communications to QIBs and IAIs permitted under the JOBS Act remain subject to potential liability under Section 12 of the Securities Act for any material misstatement or omission, as well as the generally applicable anti-fraud liability provisions of the securities laws.

- **Confidential Submission of IPO Registration Statements:** In December 2011, the SEC staff severely limited foreign private issuers’ access to confidential submission of registration statements. The JOBS Act gives that access back to EGCs, though EGCs are required to include the initial submission and all amendments that were confidentially submitted as exhibits to a publicly filed registration statement no later than 21 days before a road show. The flexibility under the December 2011 SEC staff policy for certain foreign private issuers to confidentially submit draft registration statements continues. Currently such submissions must be made in the same manner as confidential submissions by EGCs and not by electronic mail. In addition, the Division of Corporation Finance explained in a set of frequently asked questions (FAQs) released on April 16, 2012 that the availability of confidential submission under the December 2011 SEC staff policy is limited to foreign private issuers that meet the conditions outlined in the policy and either do not have EGC status or do not take advantage of any benefit available to EGCs.

On April 5, 2012, the Division of Corporation Finance announced that, pending the implementation of a system that provides for electronic transmission, confidential submissions should be submitted to the SEC in text-searchable PDF files on CDs or DVDs, or in hardcopy. The Division of Corporation Finance’s announcement is available at <http://www.sec.gov/divisions/corpfin/cfannouncements/draftregstatements.htm>.

Draft registration statements submitted confidentially must be substantially complete at the time of initial submission, including a signed audit report covering the fiscal years presented in the registration statement and exhibits.

Consistent with its current practice in respect of foreign private issuers, the Division of Corporation Finance has noted that it will defer review of any draft registration statement submitted confidentially that is materially deficient. The staff of the Division of Corporation Finance has also confirmed that the filing fee is only due when the registration statement is first filed publicly on the SEC’s EDGAR system. Further points of clarification relating to the confidential submission process are available from the Division of Corporation Finance in its list of FAQs released on April 10, 2012 at <http://www.sec.gov/divisions/corpfin/guidance/cfjumpstartfaq.htm>.

- **Audited Financial Statements and Selected Financial Data:** The JOBS Act allows EGCs to present only two years of audited financial statements in an IPO registration statement, rather than the three years that are generally

<sup>2</sup> The Division of Corporation Finance noted in its April 16, 2012 FAQs that Canadian foreign private issuers filing under the Multi-Jurisdictional Disclosure System, or MJDS, would continue to be subject to the Canadian disclosure requirements but that other provisions of Title I of the JOBS Act, such as the test-the-waters provisions and the exemption from the Sarbanes-Oxley Section 404 auditor’s attestation report, would be available to an MJDS filer that qualifies as an EGC.

required under the current rules. The JOBS Act also provides that an EGC need not present in a registration statement selected financial data for any period prior to the earliest audited period presented in its IPO registration statement rather than the five years that are generally required under the current rules. The Division of Corporation Finance explained in its April 16, 2012 FAQs that, although some of the relevant provisions of the JOBS Act refer only to the applicable disclosure rules for US domestic issuers, EGC foreign private issuers may also take advantage of these reduced disclosure requirements immediately.

- **Analyst Research Reports:** The JOBS Act changes the rules applicable to the publication of research reports relating to offerings by EGCs. Under the current rules, investment banks participating in an IPO cannot publish research in advance of the IPO or until 40 days after completion of the offering and must cease publishing research for a period of 15 days before and after the release or expiration of any lock-up agreement. There are also a variety of restrictions limiting contact between bankers and research analysts that are in place to ensure the separation of the investment banking and research functions of broker-dealers.

The changes under the JOBS Act will:

- exempt broker-dealer research reports on EGCs before, during or after offerings of an EGC's common equity (including an IPO) from being considered an offer or a prospectus under the Securities Act, even if the broker-dealers are participating in the offering;
- permit broker-dealers to issue research reports on EGCs after IPOs (without compliance with the 40-day quiet period) and before the expiration of IPO lock-up agreements; and
- allow research analysts to communicate with management in connection with the IPO of an EGC even if investment bankers are present.

It remains to be seen whether pre-deal research and the participation of research analysts in investor education will be used in the US IPO process for EGCs as they commonly are in certain non-US IPO markets. Additionally, the flexibility provided by the JOBS Act may be limited by the restrictions imposed by the Global Research Analyst Settlement entered into in 2003, to the extent they are still applicable, and concerns over 10b-5 liability, which may result in broker-dealers retaining restrictions on their own research activities.

## Changes to Ongoing Reporting Obligations of Emerging Growth Companies

The JOBS Act reduces some public company reporting and other requirements for EGCs for as long as they retain their status as such. Under the JOBS Act, a company does not qualify as an EGC if it conducted its US IPO on or before December 8, 2011. A company that has annual gross revenues of less than US\$1 billion<sup>3</sup> that qualifies as an EGC will retain its status until the earliest of:

- the last day of the fiscal year following the fifth anniversary of its IPO in the United States;
- the last day of the fiscal year during which it has gross revenues of US\$1 billion or more;

<sup>3</sup> The term "total annual gross revenues," which is used in the JOBS Act definition of EGC, is not defined in the JOBS Act. The Division of Corporation Finance indicated in one of its April 16, 2012 FAQs that "total annual gross revenues" "means total revenues as presented on the income statement presentation under U.S. GAAP (or IFRS as issued by the IASB, if used as the basis of reporting by a foreign private issuer)." The FAQ goes on to say that if a foreign private issuer prepares its financial statements in a currency other than US dollars, it should calculate total annual gross revenues using the exchange rate as of the last day of its most recently completed fiscal year.

- the date on which it has issued more than US\$1 billion in non-convertible debt during the previous three years;<sup>4</sup> and
- when it becomes a “large accelerated filer,” generally meaning that its public float is US\$700 million or more.

The most significant change to the ongoing reporting regime for foreign private issuers is that, while EGCs must continue to comply with the Sarbanes Oxley requirement to establish and maintain internal controls over financial reporting, the JOBS Act exempts EGCs (for as long as they remain EGCs) from Sarbanes-Oxley Section 404’s requirement to obtain an annual attestation report on their internal control over financial reporting from a registered public accounting firm. The existing requirement for CEOs and CFOs to certify public companies’ financial statements is not affected.

EGC foreign private issuers that prepare their financial statements in accordance with US generally accepted accounting principles (GAAP) are also permitted to delay application of any new or revised US GAAP financial accounting standard applicable to public companies until the standard becomes mandatory for private companies.

### Liberalization of Publicity for Rule 144A Offerings

In a significant change to existing securities law and practice, the JOBS Act directs the SEC, within 90 days after enactment, to revise Rule 144A to permit offers to be made to persons other than QIBs, including through general solicitation and advertising, provided that the securities are only resold to persons the seller reasonably believes are QIBs.

While some of the changes mandated by the JOBS Act are effective when it is signed into law, general solicitation and advertising in connection with Rule 144A offerings will not be permitted until the SEC revises the applicable rules. Issuers and sellers of securities should establish compliance procedures, including verification procedures to be provided by the SEC in its rules, to avoid sales to ineligible investors. Importantly, the JOBS Act has not altered the scope of the anti-fraud liability provisions of the Securities Act and the Exchange Act applicable to disclosures provided to investors, nor does it appear to address the prohibition on “directed selling efforts” in offshore offerings conducted pursuant to Regulation S under the Securities Act, which could limit the benefits of the changes for foreign private issuers conducting side-by-side Rule 144A and Regulation S offerings.

### Offerings of US\$50 Million or Less

The JOBS Act directs the SEC to create a new exemption (or modify an existing exemption, such as that provided by Regulation A) for public offerings of equity securities, debt securities and debt securities convertible or exchangeable into equity securities that, in the aggregate, do not exceed US\$50 million in any 12-month period. This exemption is expected to apply to domestic and foreign private issuers.

<sup>4</sup> The JOBS Act refers to the “previous 3-year period” and does not specify fiscal years or a rolling three-year period. It does not specify whether the debt may be private or public and whether the debt includes only debt securities or other debt, such as bank loans. In its April 16, 2012 FAQs, the Division of Corporation Finance clarified that the JOBS Act test contemplates a rolling three-year period and includes all debt securities that have been issued by an EGC in both SEC-registered and Rule 144A and other private transactions during the period. The test does not include other debt (such as bank loans). Members of the staff of the Division of Corporation Finance noted during an April 11, 2012 discussion panel sponsored by the Practising Law Institute that the test applies to issuances of debt securities and not outstanding debt securities. The JOBS Act also does not exclude refinancings from the debt test, which could lead to anomalous results.

Additional conditions to these offerings may be provided by the SEC as it may determine are necessary for the protection of investors and in the public interest. These conditions may require the issuer to prepare, electronically file with the SEC and distribute to potential investors an offering statement, including audited financial statements, and impose disqualification provisions similar to those in the Dodd-Frank Wall Street Reform and Consumer Protection Act, limiting the ability of “bad actors” to take advantage of the exemption.

Issuers that take advantage of this exemption will be required to file audited financial statements with the SEC annually and make periodic disclosure as the SEC directs, including, among other items, a description of the issuer’s business and financial condition and its corporate governance principles.

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If you wish to review further information regarding the changes to the regime governing the US capital markets effected by the JOBS Act, including details of how each of the affected laws, rules and regulations will change, you may refer to our client publication entitled “JOBS Act Will Ease Rules for IPOs and Private Placements and Reduce Compliance Burdens Post IPO” at <http://www.shearman.com/jobs-act-will-ease-rules-for-ipos-and-private-placements-and-reduce-compliance-burdens-post-ipo-03-2012/>, our client publication entitled “The JOBS Act: Changes to Existing Law / A Blackline and Annotated Reference Guide” at <http://www.shearman.com/the-jobs-act-changes-to-existing-law--a-blackline-and-annotated-reference-guide-03-2012/>, our client publication entitled “New Law Reduces Executive Compensation Disclosure Obligations and Eliminates Say-on-Pay Votes for Emerging Growth Companies” at <http://www.shearman.com/new-law-reduces-executive-compensation-disclosure-obligations-and-eliminates-say-on-pay-votes-for-emerging-growth-companies-04-02-2012/>, our client publication entitled “JOBS Act Signed Into Law” at <http://www.shearman.com/jobs-act-signed-into-law/> and our client publication entitled “SEC Division of Corporation Finance Addresses JOBS Act Questions” at <http://www.shearman.com/publications/>.

This memorandum is intended only as a general discussion of these issues. It should not be regarded as legal advice. We would be pleased to provide additional details or advice about specific situations if desired.

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