SHEARMAN & STERLING LLP

CAPITAL MARKETS

CLIENT PUBLICATION

April 17, 2012

SEC Division of Corporation Finance Addresses JOBS Act Questions

The SEC Division of Corporation Finance (the Division) issued three sets of Frequently Asked Questions (FAQs), and members of the Division staff participated in a panel discussion sponsored by the Practising Law Institute (PLI), to answer certain questions raised by the Jumpstart Our Business Startups Act, also known as the JOBS Act.[1] Although the FAQs and the statements made at the PLI panel do not have the legally binding authority of SEC rules, they provide useful guidance to market participants. The SEC has invited public comments throughout its JOBS Act rulemaking process via a web interface found at http://www.sec.gov/spotlight/jobsactcomments.shtml.

Emerging Growth Company Status

Under the Act, an emerging growth company (EGC) is a company that has total annual gross revenues of less than $1 billion and meets certain other conditions, including that it has not priced its IPO on or before December 8, 2011.[2] The Division's FAQs clarified that "total annual gross revenues" means "total revenues as presented on the income statement presentation" either under US GAAP or IFRS as issued by the IASB, if the issuer reports using IFRS.

To qualify as an EGC, a company also must not have issued, during the previous three-year period, more than $1 billion in non-convertible debt. As confirmed by the Division's FAQs, unlike certain of the other criteria for EGC status, the Act provides that this test must be met on a three-year rolling basis (and not just as of the end of a specified fiscal period). It 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) that is not in the form of securities.

[1] The Act, in the form signed into law by President Obama on April 5, 2012, is available at: http://www.gpo.gov/fdsys/pkg/BILLS-112hr3606enr/pdf/BILLS-112hr3606enr.pdf. The April 10, 2012 FAQs regarding the process of submitting registration statements to the SEC confidentially are available at: http://www.sec.gov/divisions/corpfin/guidance/cfjumpstartfaq.htm. The April 11, 2012 FAQs regarding the changes to the requirements for registration and deregistration of equity securities under the Exchange Act are available at: http://www.sec.gov/divisions/corpfin/guidance/cfjjobsactfaq-12g.htm. The April 16, 2012 FAQs regarding generally applicable questions on Title I of the Act are available at: http://www.sec.gov/divisions/corpfin/guidance/cfjjobsactfaq-title-i-general.htm.

In addition to two attorneys in private practice, participants in the April 11, 2012 PLI panel included the following members of the Division staff: Meredith B. Cross (Director), Lona Nallengara (Deputy Director, Legal and Regulatory Policy) and Shelley E. Parratt (Deputy Director, Disclosure Operations). The members of the Division staff indicated during the PLI panel that questions regarding the application of the Act to equity research on EGCs would be addressed by the staff of the Divisions of Corporation Finance and Trading & Markets in the future.

[2] The Division's FAQs explained that an EGC should indicate on the cover of the prospectus for any securities offering that it is an EGC.

According to the Division's FAQs, for confidential submissions of draft registration statements and amendments, a company must qualify as an EGC at the time of each submission. As the FAQs further explain, based on Rule 401(a) under the Securities Act, so long as a company meets the criteria for EGC status at the time of the initial public filing of its registration statement, the disclosure provisions for EGCs would apply to it throughout the registration process until effectiveness, even if it loses its EGC status before effectiveness.

For other activities, such as testing the waters or publishing a research report on an EGC, EGC status must be tested at the time of the relevant activity. As discussed in the PLI panel, for purposes of shelf registration, EGC status must be tested at the time of the initial filing and at the time of the annual update of the shelf registration statement.

Confidential Submission of Registration Statements by Emerging Growth Companies

Issuers Eligible to Use Confidential Submission. Under the Act, an EGC that has not yet conducted an IPO may confidentially submit its Securities Act registration statements to the SEC for review prior to public filing. An IPO is defined as the date of the first sale of an issuer's common equity securities registered under the Securities Act. The Division's FAQs caution that certain offerings, such as an offering of common equity securities to employees pursuant to a Form S-8 registration statement or a selling shareholder's secondary offering of common equity securities using a resale registration statement, may constitute an EGC's IPO, as defined in the Act, and thus preclude access to the confidential submission process. SEC-registered sales of securities other than common equity securities, such as debt securities, do not disqualify an EGC from using the confidential submission process.

Foreign private issuers (FPIs) that meet the criteria for EGC status are eligible to use the confidential submission process for EGCs, subject to the same conditions as domestic EGCs. In addition, as the Division has previously announced, certain FPIs (including EGCs) may continue to confidentially submit registration statements to the SEC for review if they meet other specified conditions, such as a listing on a non-US securities exchange. However, the Division's FAQs limit the pre-JOBS Act confidential submission process for FPIs to those FPIs that either do not have EGC status or do not take advantage of any benefit available to EGCs.

Procedure and Requirements Applicable to the Confidential Submission Process. The Division provided guidance on the procedure and requirements for confidential submission, including the following:

- Filing fees are due when a registration statement is first publicly filed and do not need to be paid upon a confidential submission.
- Draft registration statements that are confidentially submitted need not be signed or include the consent of auditors and other experts and may omit certain other information, such as the public offering price and other offering-related information. Otherwise, they must be substantially complete, including a signed audit report covering the financial statements in the registration statement and exhibits.
- If an EGC is currently in registration with the SEC, it may switch to the confidential submission process, choose to comply with the reduced disclosure requirements applicable to EGCs, or both, for future amendments to its registration statement.
- The Division currently requires confidential submissions to be made either in paper or preferably on a CD or DVD containing a text-searchable PDF file, but a process for electronic confidential submissions is expected to be available in the near future.

- The confidential submission of a registration statement does not constitute the "filing" of a registration statement for purposes of the publicity restrictions that apply prior to the filing of a registration statement. As a result, EGCs will, for example, be limited in their ability to respond to questions from the press or employees that have learned about a confidential submission.
- In connection with the confidential submission process, EGCs do not need to make a confidential treatment request under Rule 83 to preserve confidentiality.

In the PLI panel discussion, the members of the Division staff indicated that registration statements that are submitted confidentially by EGCs will go through substantially the same review process at the same speed as publicly filed registration statements, assuming the requirements for submission and content of the registration statement have been met.

Interplay of Confidential Submission, Road Shows and Testing the Waters

The Act requires that any confidential submission of a registration statement and subsequent confidential amendments to the registration statement by an EGC be publicly filed with the SEC no later than 21 days before the EGC conducts a "road show."[3] The Act also provides that EGCs and any person authorized to act on their behalf may test the waters in connection with any contemplated securities offering, meaning that they may have communications with potential investors that are QIBs and institutional accredited investors (IAIs) to determine their interest in an offering prior to the filing of a registration statement. The Division indicated in its FAQs that it would not consider testing-the-waters communications, so long as they are conducted in accordance with the Act, to be a road show. As a result, testing the waters with QIBs and IAIs should have no impact on the ability of EGCs to use the confidential submission process.

If an EGC that has made a confidential submission does not conduct a traditional road show and engages only in permissible testing-the-waters communications, the Division requires it to publicly file its confidentially submitted registration statement and all subsequent amendments at least 21 days in advance of effectiveness of its registration statement.

Testing-the-Waters Communications

At the PLI panel, the members of the Division staff confirmed that written testing-the-waters communications, to the extent they are used, would currently not be subject to filing with the SEC. However, they also indicated an interest in learning about the information that is provided to QIBs and IAIs as part of the testing-the-waters process, with a view to ensuring that any material information provided during that process is also made available to investors in the public offering.

Clarification of Standards Applicable to Emerging Growth Companies

The Division's FAQs address several questions regarding the disclosure standards applicable to EGCs. If an EGC completed its IPO after December 8, 2011 and prior to April 5, 2012, it may choose to use the disclosure standards applicable to EGCs in its subsequent periodic reports to the SEC. An EGC is allowed to elect to rely only on some of the reduced disclosure

[3] The Division has instructed that previous confidential submissions of the registration statement and any amendments should be attached as exhibits to an EGC's initial public filing of the corresponding registration statement.

requirements for EGCs and otherwise comply with non-EGC disclosure rules. It is only with regard to the delayed application of new or revised financial accounting standards applicable to public companies that an EGC must either delay application of all such standards or exercise its one-time right to adopt all such standards at the time of its initial filing. The Division specified that an EGC that is planning to submit a draft registration statement confidentially should notify the Division review staff of its choice either to delay application of or adopt the standards in its initial confidential submission. If it is already an SEC-reporting company or has filed a registration statement, an EGC should make and disclose its choice regarding the financial accounting standards in its next filing with the SEC.

The Division also provided guidance in its FAQs regarding the financial statements that an EGC is required to present. In registration statements other than its IPO registration statement, an EGC need not present audited financial statements for any period prior to the earliest audited period presented in its IPO registration statement. In addition, if under Regulation S-X an EGC would be required to present three years of financial statements of another entity, such as an acquired business, an EGC need only present two years of financial statements for that entity. Even though the Act refers to the relevant rules for domestic issuers in limiting the required selected financial data and MD&A for EGCs, according to the Division's FAQs, FPIs may also take advantage of these accommodations immediately.

Changes to the Requirements for Exchange Act Registration for Private Companies

The Act increased the threshold for the number of shareholders at which a private company is required to register any class of its equity securities with the SEC under the Exchange Act from 500 or more shareholders of record to either 2,000 shareholders of record or 500 shareholders of record who are not accredited investors. The corresponding threshold for banks and bank holding companies was increased to 2,000 shareholders of record. The Act also increased the threshold for deregistration of any class of equity securities of banks and bank holding companies under the Exchange Act to 1,200 shareholders of record.

Companies may immediately exclude from the calculation of the shareholders of record of a class of their equity securities persons who received the securities pursuant to an employee compensation plan in a transaction exempt from registration under the Securities Act.[4] However, the members of the Division staff explained in the PLI panel that their current view is that persons who received their securities through a transfer from a person who had received the securities in an exempt transaction from an employee compensation plan would be included in the shareholder of record calculation.

[4] Section 503 of the Act requires that the SEC specify safe harbor provisions that issuers can follow when determining whether holders of their securities received the securities pursuant to an employee compensation plan in transactions that were exempt from registration under the Securities Act. The SEC has not yet specified those provisions, but the Division clarified that absence of a safe harbor does not prevent issuers from taking advantage of the change to Exchange Act Section 12(g)(5) that permits exclusion of persons who received the securities pursuant to an employee compensation plan in a transaction exempt from registration under the Securities Act.

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.

If you wish to receive more information on the topics covered in this publication, you may contact your regular Shearman & Sterling contact person or any of the following:

Abigail Arms
Washington, D.C.
+1.202.508.8025
aarms@shearman.com

Matthew Bersani
Hong Kong
+852.2978.8096
matthew.bersani@shearman.com

Robert Ellison
São Paulo
+55.11.3702.2220
robert.ellison@shearman.com

Robert Evans III
New York
+1.212.848.8830
revans@shearman.com

Jason R. Lehner
Toronto
+1.416.360.2974
jlehner@shearman.com

Richard J.B. Price
London
+44.20.7655.5097
rprice@shearman.com

Antonia E. Stolper
New York
+1.212.848.5009
astolper@shearman.com

John D. Wilson
San Francisco
+1.415.616.1215
jwilson@shearman.com