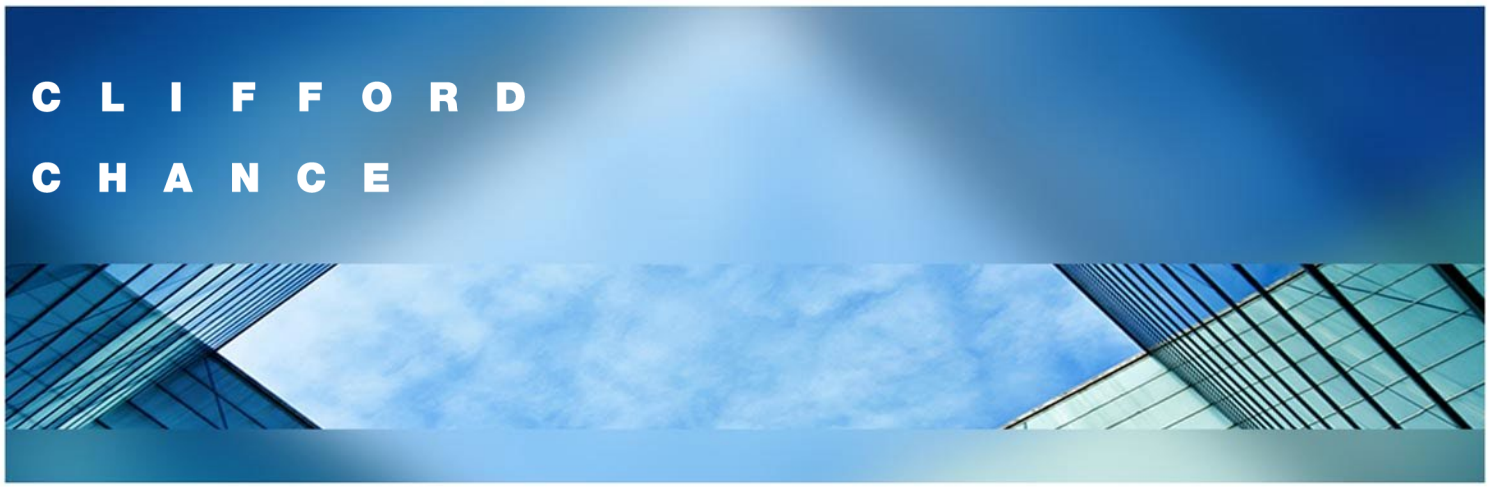

SEC ADOPTS RULES TO MODERNIZE EXEMPT OFFERINGS TO PROMOTE CAPITAL RAISING

On November 2, 2020, the Securities and Exchange Commission (the "SEC") amended its rules to modernize and harmonize its exempt offerings framework to promote capital raising while preserving investor protections. The SEC recognized the growing appeal of private investments and the existing complexity of its exempt offering framework and adopted this comprehensive and integrative framework to broaden access to capital markets for issuers and to the exempt offering market for investors. The amendments will impact offerings under Section 4(a)(2), Regulation D, Regulation S, Regulation A, Regulation Crowdfunding and all other exempt private offerings.

Key issues

- The SEC has modernized and harmonized its exempt offerings frameworks.
- Amended Rule 152 introduces a new integration doctrine framework that applies to all registered and exempt offerings.
- The integration doctrine's traditional five-factor test will be supplanted with a more concise general principle.
- Four non-exclusive integration safe harbors will be introduced.
- Under certain conditions, an issuer will be permitted to make a "testing the waters" communication and participate in "demo days" for exempt offerings.
- Larger offering size amounts will be permitted for offerings exempt under Rule 504, Regulation A and Regulation Crowdfunding.

One aspect of these amendments was the introduction of a new integration doctrine framework reflected in amended Rule 152, which will consolidate a patchwork of SEC rules and guidance that has developed over the last several decades. The integration doctrine seeks to prevent issuers from utilizing a series of smaller exempted offerings that is effectively one consolidated single offering in an attempt to avoid registration of securities. The amended Rule 152 will supplant the existing integration framework with a concise general principle and four non-exclusive safe harbors.

In addition to updating the integration doctrine, the new rules also:

- expand the scope of permissible offering communications including testing the waters communications and "demo days" for exempt offerings;
- increase the offering size amounts available to issuers under Rule 504, Regulation A and Regulation Crowdfunding offerings; and
- generally simplify and harmonize the exempt offering framework.

This client briefing highlights certain of the amendments that we think would be of interest to our clients that conduct exempt private offerings on a regular basis.

History of "Integration"

The concept of integration refers to the circumstances the SEC uses to determine whether separate securities offerings should be combined and treated as a single offering for purposes of establishing the availability of an exemption from the registration requirements of the Securities Act. The integration doctrine emerged over the decades following the adoption of the Securities Act of 1933, as amended (the "Securities Act"), and eventually developed into a subjective five-factor test by the late 1960s. This five-factor test inquired whether securities offered in multiple offerings (i) were part of a single plan of financing, (ii) were of the same class of security, (iii) occurred at or about the same time, (iv) consisted of the same type of consideration, and (v) were made for the same general purpose. The SEC later added various safe harbors, such as a six-month separation window for Regulation D offerings; issued guidance tailored to specific circumstances; and promulgated additional rules, including Rules 152 and 155, oftentimes each with their own variant of integration or safe harbors. Eventually, the integration doctrine became a difficult to navigate web of principles and guidelines, which proved difficult for many issuers when structuring private offerings and raising capital.

Key issues

- The general principle will determine whether the particular facts and circumstances indicate that the offering was (i) properly registered or (ii) exempt from registration, subject to two specific circumstances.
- A new 30 day safe harbor will apply to all offerings, subject to certain qualifications.

Updating the "Integration" Framework - Amended Rule 152

The SEC adopted amended Rule 152 to combine the patchwork of integration rules and guidance into a single simplified cohesive framework. In this new framework, integration analysis for all public and private offerings will be determined by either a general principle or one of four non-exclusive safe harbors. The rule (whether under the safe harbors or the general principle), however, will not protect offerings that are part of a plan or scheme to evade the registration requirements of the Securities Act. Thus, for example, an issuer may not use a general solicitation from one offering to identify investors for a subsequent exempt offering that prohibits such communication.

Rule 152(a) – General Principle of Integration

Rule 152(a) describes a new general principle that will govern the evaluation of whether offerings that do not satisfy any of the four safe harbors (described below) should be integrated. The general principle will no longer be based on a five-factor test; rather, an issuer will now analyze whether the particular facts and circumstances indicate that the offering was either (i) properly registered under the Securities Act or (ii) met the qualifications for exemption from registration.

If the issuer establishes (i) or (ii) above, then Rule 152(a) lays out two additional applications which would require further analysis in order to conclude that the offerings should not be integrated:

- First under Rule 152(a)(1), for a private offering that is exempted under the Securities Act but prohibits general solicitation, the issuer must further possess a reasonable belief, based on facts and circumstances, that the issuer:
    - did not solicit any purchasers through a general solicitation; or
    - had a substantive pre-existing relationship with any purchaser that may have been solicited.

- The pre-existing relationship may have been established prior to the commencement of the offering or through a third party, such as a registered broker-dealer or investment advisor. The relationship must be one where the issuer has sufficient information to evaluate and has made a determination from such person's financial circumstances and sophistication on whether the offeree is an accredited or sophisticated investor. Self-certification of financial status and sophistication by a purchaser will not be sufficient to establish a substantive relationship in the SEC's view.

- Second, under Rule 152(a)(2), for two or more concurrent private offerings by the same issuer in which general solicitations are permitted, if one offering's materials describes the material terms of the other offering relying on a different exemption, then that offering must comply with the requirements for, and restrictions on, the exemption by which the other offering relies upon, including any legend requirements and communications restrictions.

  - So, for example, if an issuer conducting an offering pursuant to Rule 506(c) of Regulation D describes in a widely circulated private placement memorandum the terms and conditions of a concurrent Regulation A or Regulation Crowdfunding offering by the same issuer, then the Regulation D offering must also comply with all the requirements and restrictions of Regulation A or Regulation Crowdfunding, as applicable.

Key issues

- Employee benefit plans and offshore offerings will not be integrated with other offerings.
- Issuers will have more flexibility to raise capital under certain circumstances in the days leading up to a public offering.
- Private offerings in which general solicitations are permitted will not be integrated with prior offerings that have been terminated or completed.
- Issuers should consult the amended rule for a list a non-exclusive factors to determine when an offering is deemed commenced, completed or terminated.

Rule 152(b) – Non-Exclusive Safe Harbors from Integration

New Rule 152(b) sets forth four non-exclusive safe harbors from any further integration analysis in an attempt to provide bright line rules to simplify compliance:

Rule 152(b)(1) - 30 Day Window

The SEC will replace the various safe harbors regarding time periods between a variety of exempt offerings, which had ranged from 30 days to six months, with a single 30-day window. This means that any offerings (registered or exempt) conducted either (i) 30 days before the commencement of another offering or (ii) 30 days after the termination or completion of another offering will not be integrated into the other offering. As a result current Rule 155 has been removed as Rule 152(b)(1) supersedes it.

This safe harbor, however, will not apply to private offerings for which general solicitations are prohibited, unless the provisions of Rule 152(a)(1) apply (i.e, the issuer reasonably believes that:

- none of the purchasers had been solicited by the issuer by a prior offering in question; or
- the issuer had a substantial pre-existing relationship with such purchasers.)

The SEC also amended Rule 506(b) of Regulation D, to limit the number of non-accredited investors purchasing in a Rule 506(b) offering to no more than 35 within

a 90-day calendar period. This will prevent issuers from making numerous offers to non-accredited investors within a short period of time.

Rule 152(b)(2) - Employee Benefit Plans and Offshore Offerings

Offers and sales made in compliance with Rule 701 pursuant to an employee benefit plan or offshore offerings conducted in accordance with Regulation S will not be integrated with any other concurrent offering. An issuer, however, must continue to ensure that offerings made offshore do not constitute directed selling efforts to U.S. investors and comply with all aspects of Regulation S. For example, an issuer must be careful not to post its soliciting materials to foreign investors in a Regulation S offering on the same website it uses to reach U.S. investors. However, the SEC did clarify that it does not believe that general solicitation activity for exempt domestic offerings would preclude reliance on Regulation S for concurrent offshore offering and reaffirmed its existing guidance.

Rule 152(b)(3) - Registered Offerings Following Certain Private Offerings

Under the amended rule, a registered offering will not be integrated with a prior offering that was terminated or completed if such offering:

- did not permit a general solicitation;
- permitted a general solicitation but was made to only qualified institutional buyers ("QIBs") and institutional accredited investors ("IAIs"); or
- permitted a general solicitation but was terminated or completed more than 30 days prior to the commencement (or first offer) of the registered offering.

The SEC believes that capital raising around the time of an IPO, including immediately before the filing of a registration statement is often critical for issuers seeking to raise sufficient funds to continue to operate while the IPO process is ongoing. Under this safe harbor, an issuer will have greater flexibility to conduct offerings prior to the filing of a registration statement.

Rule 152(b)(4) - Private Offerings Permitting General Solicitations Following a Completed Offering

Finally, exempt private offerings in which general solicitations are permitted will not be integrated with any prior offering that has been terminated or completed. So for example, an offering can begin using the Rule 506(b) exemption and change to Rule 506(c) so long as it complies with all the requirements of Rule 506(c). This effectively terminates the 506(b) offering. Additionally, the issuer can use the same offering materials for these different offerings so long as it satisfies the disclosure and other requirements of each applicable exemption. This safe harbor expands the current integration safe harbors in Regulation A, Rules 147 and 147A, Rule 506(c) and guidance for Regulation Crowdfunding.

Rule 152(c) and (d) - Non-Exclusive Factors to Determine when an Offering is Commenced, Completed or Terminated

In addition to the general principle and safe harbors described above, the amended Rule 152 also provides a list of non-exclusive factors to determine when an offering has been "commenced" or "completed or terminated".

New Rule 152(c)

New Rule 152(c) states that for purposes of Rule 152(a) and (b), an offering will be deemed commenced at the time of the first offer of securities in the offering by the issuer or its agents and lists factors covering different registered and exempt offerings. In particular, the commencement of a registered continuous offering will begin with the filing of the registration statement. On the other hand, the filing of a shelf registration statement will not commence an offering. Rather, commencement will begin with public efforts by the issuer or its agents and underwriters to offer and sell securities under such registration statement. Generally for other exempt offerings, the offering commences when the issuer first makes an offer of its securities in reliance on the particular exemption.

New Rule 152(d)

New Rule 152(d) states that for purposes of Rule 152(a) and (b), an offering will generally be deemed terminated or completed at the time the issuer and its agents enter into binding contracts to sell all securities to be sold under such offering or cease efforts to further offers to sell the issuer's securities under such offering. For a registered transaction, this occurs upon:

- the withdrawal or sunsetting after three years of the registration statement;
- a SEC order declaring the registration abandoned or the filing of a prospectus supplement stating the offering is terminated or completed; or
- a Form 8-K or other public disclosure informing the market that the offering is terminated or completed.

Issuers should be sure to consult the complete list of factors under Rule 152(c) and (d) when conducting an integration analysis.

Integration Analysis

The chart below describes the new integration framework under amended Rule 152.

Rule 152	**Offerings Not Integrated**
Does the offering fall under one of the four non-exclusive safe harbors?	

Safe Harbor #1
Rule 152(b)(1)
	The offering occurred either 30 calendar days (i) before the commencement or (i) after the termination or completion of an offering and:
	• general solicitations are permitted; or
	• general solicitations are not permitted, but the issuer reasonably believes from the facts and circumstances that:
	  ○ purchasers were not solicited by the issuer; or
	  ○ purchasers that were solicited had a substantial pre-existing relationship with the issuer.

Rule 152	Offerings Not Integrated
	If the offering was conducted pursuant to Rule 506(b) Regulation D, no more than 35 accredited investors have been solicited in a 90 day period.
Safe Harbor #2 Rule 152(b)(2)	**The offering is made pursuant to Rule 701 or other employee benefits plans or is conducted offshore in accordance with Regulation S.**
Safe Harbor #3 Rule 152(b)(3)	**The offering is a public offering in which the registration statement is filed after an offering that:** • did not permit a general solicitation; • permitted a general solicitation but was made to only QIBs and IAIs; or • permitted a general solicitation but was terminated or completed more than 30 days prior to the commencement of the registered offering.
Safe Harbor #4 Rule 152(b)(4)	**The offering is a private offering for which general solicitation is permitted and follows any other terminated or completed offering.**
If not, can it be concluded from the general principle that the offerings should not be integrated?	
General Principle Rule 152(a)	**The particular facts and circumstances indicate that the offering was either (i) properly registered under the Securities Act or (ii) exempt from registration, and if the offering:**

Rule 152(a)(1)	• **is private and general solicitations are prohibited, but the issuer reasonably believes from the facts and circumstances that:**
	  ○ purchasers were not solicited by the issuer; or
	  ○ purchasers that were solicited had a substantial pre-existing relationship with the issuer.

Rule 152(a)(2)	• **is private and concurrently offered with another offering, [both of which general solicitations are permitted, and such offering's general solicitation offering materials:**
	  ○ do not describe the other offering; or
	  ○ describes the other offering and the offering complies with all requirements and restrictions under the exemption being relied upon by the other offering, including any legend requirements and communications restrictions.

Expanded Testing the Waters/General Solicitation Communications

Current Securities Act Rule 163B permits issuers and those authorized to act on their behalf to gauge market interest in a registered offering through discussions with QIBs and IAIs prior to, or following, the filing of a registration statement. Regulation A also permits issuers to test the waters with, or solicit interest in a potential offering from, the general public either before or after the filing of a registration statement. These communications are generally known as "testing the waters" communications and are subject to the antifraud provisions of the Securities Act.

Key issues

- Issuers will now be permitted to "test the waters" in exempt private offerings.
- No solicitation, acceptance of consideration, or binding commitments are permitted until the exemption on which the issuer will rely is determined.
- For Regulation A or Regulation Crowdfunding offerings, generic solicitation materials must be an exhibit to the offering materials filed with the SEC if offering is commenced within 30 days of the communication.
- For Rule 506(b) offerings, the generic solicitation must be provided to purchasers if securities are sold within 30 days to a non-accredited investor.

New Rule 241 – "Testing the Waters" – Exempt Offerings

New Rule 241 permits an issuer or any person authorized to act on behalf of an issuer to communicate orally or in writing to determine whether there is any interest in a contemplated offering of securities exempt from registration under the Securities Act. Such generic solicitation of interest will be deemed an offer of securities for sale for purposes of the antifraud provisions of the Securities Act. No solicitation or acceptance of consideration nor any commitment, binding or otherwise, from any person is permitted until the issuer makes a determination as to the exemption on which it will rely and commences the offering in compliance with such exemption. Issuers should note that if the generic solicitation is deemed to be general solicitation and the issuer pursues a private offering not permittting general solicitation, the integration analysis will need to be conducted.

Rule 241 further requires the generic testing-the-waters materials to state:

- the issuer is considering a private offering but has not determined the specific exemption it intends to rely on;
- no money or other consideration is being solicited, and if sent in response, will not be accepted;
- no offer to buy the securities can be accepted and no part of the purchase price can be received until the issuer determines the exemption to be used and the requirements of such exemption are met; and
- a person's indication of interest involves no obligation or commitment of any kind.

Regulation A or Regulation Crowdfunding and Rule 506(b) "Testing the Waters"

For a Regulation A or Regulation Crowdfunding offering using Rule 241, the generic solicitation materials must be made publicly available as an exhibit to the offering materials filed with the SEC if such offering is commenced within 30 days of the generic solicitation.

For a Rule 506(b) offering, the generic solicitation materials must be provided to purchasers of such offering if securities are sold within 30 days of the generic solicitation of interest to any purchaser that is not an accredited investor.

State blue sky laws still must be complied with in respect of these generic solicitations of potential investors.

Benefits of New Rule 241

This rule greatly expands the flexibility of issuers to gauge potential interest in a private offering before incurring the time and costs of pursuing such offering and should expand capital market activity in the private markets.

New Rule 148 – "Demo Days"

New Rule 148 states that "demo day" communications will not be considered a general solicitation. "Demo days" and other similar events are generally organized by a group (such as a university, state or local government, angel investor or incubator) that invites issuers to present their businesses to potential investors with the aim of securing investments. For virtual "demo days" participation is limited to:

- individuals who are members or otherwise associated with the event sponsor;
- individuals the sponsor reasonably believes are accredited investors; or
- individuals who have been invited by the sponsor based on industry or investment-related experience deemed relevant by the sponsor in good faith and disclosed in the public communication about the event.

Multiple investors must attend the event. In addition, the investors are allowed to convey only:

- notification that the issuer is in the process of offering or planning to offer securities;
- the type and amount of securities being offered;
- the intended use of proceeds; and
- the unsubscribed amount in an offering.

Further, the sponsor will not be permitted to:

- make investment recommendations or provide investment advice to the attendees of the event;
- engage in any investment negotiations between the issuer and investor at the event;
- charge attendees of the event any fees, other than reasonable administrative fees;
- receive any compensation for making introductions; or
- receive any compensation that would require it to register as a broker or dealer under the Securities Exchange Act or 1934, as amended or an an investment advisor under the Investment Advisers Act of 1940, as amended.

Key issues

- Issuers may participate in "demo days", subject to certain requirements under new Rule 148.
- The Release also increases the amounts that may be offered in certain exempt offerings.

Other Changes

The SEC amended Regulation A, Regulation Crowdfunding and Rule 504 to increase the amounts that can be offered within a 12-month period as follows:

- **Tier 2 Regulation A Offerings**: from $50 million to $75 million;
- **Rule 504**: from $5 million to $10 million; and

- **Regulation Crowdfunding**: from $1.07 million to $5 million.

In addition, the amendments set forth in the final rule will:

- align the bad actor disqualification provisions that apply in Regulation D, Regulation A and Regulation Crowdfunding;
- permit a purported accredited investor to verify its accredited investor status by providing a written representation to the issuer for a five-year period since the financial records of such investor were reviewed by the issuer, so long as the issuer is not aware of anything impacting that investor's accredited investor status;
- make information that issuers must provide to non-accredited investors under Rule 506(b) and Regulation A equivalent; and
- remove the "competitive harm" standard in information permitted to be redacted under Items 601(b)(2)(10) of Regulation S-K if the information is of a type that the issuer both customarily and actually treats as privileged or confidential and is not material.

The amendments take effect 60 days after publication in the Federal Register.

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