

SEC Takes Another Step to Expand Private Offerings

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Last week, the Securities and Exchange Commission **proposed** broad changes to the current private offering framework. Recognizing the growing market for private investments, this is the latest in a series of recent actions by the SEC (including proposals to expand “**testing the waters**” communications and **accredited investor** definitions) intended to broaden access to capital markets for issuers and access to the exempt offering market for investors. The proposal incorporates a number of comments received by the SEC from Davis Polk and others, such as the inclusion of bright-line rules. We believe the proposal is a step in the right direction of easing and clarifying the application of rules for primary offerings that are exempt from registration.

The SEC is soliciting comments on the proposal until 60 days after publication in the Federal Register.

Highlights of the Proposal

The proposal aims to both streamline the current regime of rules and guidance governing exempt offerings and to broaden the availability of such offerings. Highlights of the proposal include:

- Streamlining and clarifying the rules governing “integration” of private and public offerings, including establishing four new safe harbors;
- Expanding general solicitation exemptions, including for “demo days”;
- Increasing the size of offerings exemptions available to issuers under Rule 504, Regulation A and Regulation Crowdfunding offerings; and
- Harmonizing certain disclosure and eligibility requirements between exemptions.

Simplified Integration Rules

The proposal would simplify the rules for integrating private and public offerings, which currently include a patchwork of SEC rules, staff guidance and market practice that have evolved over a number of years. Under the proposal, current Rule 152 would be amended to offer both a number of specified safe harbors from integration and, where no safe harbor is available, a principles-based approach to determine whether an exemption from registration is available for a particular offering.

The proposal includes four non-exclusive safe harbors from integration:

Safe Harbor 1	Offerings made more than 30 calendar days before or after any other offering would not be integrated with that offering, <i>provided</i> that for an exempt offering the purchasers: <ul style="list-style-type: none">• were not solicited through a general solicitation, or• had previously established a substantive relationship with the issuer.
Safe Harbor 2	Offers and sales made in compliance with Rule 701, pursuant to an employee benefit plan, or in compliance with Regulation S would not be integrated with other offerings.
Safe Harbor 3	An offering for which a registration statement has been filed would not be integrated with another offering if made subsequent to:

	<ul style="list-style-type: none"> • a terminated or completed offering for which general solicitation is not permitted; • a terminated or completed offering for which general solicitation is permitted and made only to qualified institutional buyers and institutional accredited investors; or • an offering that terminated or completed more than 30 calendar days prior to the commencement of the registered offering.
Safe Harbor 4	Offers and sales made in reliance on an exemption for which general solicitation is permitted would not be integrated with another offering if made subsequent to any prior terminated or completed offering.

If none of these safe harbors were available for an offering, revised Rule 152 would codify existing SEC guidance on integration by requiring an issuer to consider the particular facts and circumstances of each offering pursuant to a general principle of integration.

Expanded Testing the Waters Exemptions

Exemption for “Demo Days”

Under the proposal, “demo days” and similar events would be exempt from the definition of general solicitation. While current rules include an exemption that allows issuers to use general solicitation for exempt offerings, in order to qualify the issuers must take reasonable steps to verify that the purchasers are accredited investors. The proposed exemption is a reflection of current market practice in which startup companies often meet with larger groups of angel investors and others to present their businesses. Recognizing this, the proposal would deem communications made by an issuer not to be general solicitations if they were made in connection with a seminar or meeting by a college, university, or other institution of higher education, a local government, a nonprofit organization, or an angel investor group, incubator, or accelerator sponsoring the seminar or meeting.

In order to avail itself of the exemption, the issuer would not be permitted, among other things, to make investment recommendations, engage in investment negotiations or charge fees to attend the event. In addition, advertising for the event would not be allowed to reference an offering and information conveyed at the event regarding the offering would be limited to: (i) notification of the planned offering; (ii) the type and amount of securities being offered; and (iii) the intended use of proceeds.

General Solicitation of Interest Exemption

When the SEC expanded the “testing the waters” flexibility to all issuers in September 2019, it provided that companies would not be precluded from conducting a private placement in lieu of a registered offering after testing the waters pursuant to the new rule. This proposal goes further by including a new exemption that would permit an issuer to use a generic solicitation of interest materials for an offer of securities prior to making a determination as to the exemption under which the offering may be conducted. Certain conditions would need to be met under the proposal, including a legend on the materials used with certain disclaimers. The anti-fraud provision of the federal securities laws would apply to these solicitations of interest.

Depending on the method of dissemination of the information, such communications could be considered a general solicitation. The proposal would provide an exemption from registration only with respect to the general solicitation of interest, not for the private offering. In the event that the communication was deemed a general offering, the issuer would need to rely on a private offering exemption, such as the new

safe harbor which would require waiting 30 days following the termination of the solicitation to commence a private offering.

The proposal would require that where the issuer sells securities pursuant to one of the safe harbors within 30 days of a generic solicitation of interest, it would be required to provide any purchaser who is not an accredited investor to with any written communications used prior to the sale. If the subsequent offering is made pursuant to Regulation A or Regulation Crowdfunding, the generic solicitation materials would be required to be filed with the SEC.

Expanded Method of Verification

The proposal would expand the methods by which an issuer may verify accredited investor status by allowing an issuer to establish that an investor for which the issuer previously took reasonable steps to verify as an accredited investor remains an accredited investor as of the time of a subsequent sale if the investor provides a written representation to that effect and the issuer is not aware of information to the contrary.

Increased Offering and Investment Exemptions

The proposal would increase the offering and investment limits allowed under Regulation A, Regulation Crowdfunding and Rule 504 of Regulation D. The following chart summarizes the current and proposed offering and investment limits.

	Offering Limits		Investment Limits	
	Current Rules	Proposed Rules	Current Rules	Proposed Rules
Regulation A: Tier 1	\$20 Million	\$20 Million	None	None
Regulation A: Tier 1	\$50 Million	\$75 Million	<i>Accredited investors: no limits</i> <i>Non-Accredited Investors: limits based on the greater of an income or net worth standard</i>	<i>Accredited investors: no limits</i> <i>Non-Accredited Investors: limits based on the greater of an income or net worth standard</i>
Regulation Crowdfunding	\$1.07 Million	\$5 Million	<i>All investors: limits based on the lesser of an income or net worth standard</i>	<i>Accredited investors: no limits</i> <i>Non-Accredited Investors: limits based on the greater of an income or net worth standard</i>

	Offering Limits		Investment Limits	
	Current Rules	Proposed Rules	Current Rules	Proposed Rules
Rule 504 of Regulation D	\$5 Million	\$10 Million	None	None

Harmonization of Disclosure Requirements

For Regulation D offerings by non-reporting companies that include non-accredited investors, the proposal would align the disclosure requirement with the less burdensome disclosure requirements of Regulation A. The proposal would also simplify Regulation A by aligning it with the rules for registered offerings regarding the redaction of confidential information in material contracts, permitting draft offering statements to be made public on EDGAR, permitting incorporation by reference on Form 1-A, and permitting the declaration of a post-qualification amendment as abandoned.

If you have any questions regarding the matters covered in this publication, please contact any of the lawyers listed below or your usual Davis Polk contact.

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