

Changes to SEC Exempt Offering Rules – Regulation A and Regulation D

In November of 2020, the Securities and Exchange Commission (SEC) voted to amend its rules in order to harmonize, simplify, and improve the exempt offering framework that it believed had become too complex. These amendments became effective in March of 2021 and will promote capital formation, expand investment opportunities, and preserve investor protections.

The SEC amended rules that are established under the Securities Act of 1933—specifically Regulation A and Rule 504 of Regulation D. Although these changes will affect many exams, they will primarily impact the following exams:

FINRA	NASAA
<ul style="list-style-type: none">▪ SIE▪ Series 7▪ Series 10▪ Series 24▪ Series 79	<ul style="list-style-type: none">▪ Series 65▪ Series 66

Regulation A

Regulation A is an exempt offering provision that's available to both U.S. and Canadian issuers and allows these companies to raise a limited amount of capital without being required to satisfy the full SEC registration process. In 2012, as a result of the JOBS Act, the offering limits were increased under what was referred to as Regulation A+. Since these changes were incorporated into Regulation A, most securities professionals still refer to the exemption as Regulation A or Reg A.

Regulation A has two tiers; however, the change only affects Tier 2. Under the Tier 2 exemption, the maximum offering has been increased to \$75 million (from \$50 million) in a 12-month period. Of the \$75 million, no more than \$22.5 million can be sold by selling shareholders (which is consistent with the 30% maximum from selling shareholders). The Tier 1 exemption remains unchanged at a limit of \$20 million over a 12-month period, with no more than \$6 million from selling shareholders.

Regulation D

Regulation D is a safe harbor for exempt offerings that are commonly referred to as *private placements*. The SEC's amendment applies to Rule 504 of Regulation D and now allows for a maximum offering of \$10 million (increased from \$5 million).

The following provisions apply to both Regulation A and Regulation D exemptions:

- Disqualification if *Bad Actors* are associated with the offering
 - Bad Actors are defined as persons who, within the last 10 years, have a criminal conviction of any felony or misdemeanor in connection with the purchase or sale of any security, as well as any persons who are subject to a suspension or expulsion of membership with a securities self-regulatory organization (e.g., FINRA).
- Blank check companies and business development companies are prohibited from raising capital using these methods.
 - A special purpose acquisition company (SPAC) is a type of blank check company that raises capital to finance a merger or acquisition within a specified timeframe.

Listed below is a summary of both Regulation A and Regulation D along with additional information regarding the exemptions:

Regulation A

Tier 1	Tier 2
▪ Maximum offering size is \$20 million	▪ Maximum offering size is \$75 million
▪ Maximum offering by selling shareholders is \$6 million (30% of maximum offering)	▪ Maximum offering by selling shareholders is \$22.5 million (30% of maximum offering)
▪ Offering is subject to state registration or blue-sky filing	▪ Offering is NOT subject to state registration or blue-sky filing
▪ Issuer files Form 1-A with SEC which includes unaudited financial statements	▪ Issuer files Form 1-A with SEC which includes audited financial statements
▪ No resale restrictions	▪ No resale restrictions
▪ Permits general solicitation prior to filing (test-the-waters) and after offering documents are filed	▪ Permits general solicitation prior to filing (test-the-waters) and after offering documents are filed

Regulation D

Rule 504	Rule 506
<ul style="list-style-type: none"> ▪ Maximum offering size is \$10 million 	<ul style="list-style-type: none"> ▪ Maximum offering size is unlimited
<ul style="list-style-type: none"> ▪ Offering is NOT subject to SEC or state registration requirements 	<ul style="list-style-type: none"> ▪ Offering is NOT subject to SEC or state registration requirements
<ul style="list-style-type: none"> ▪ Issuer files Form D with SEC <ul style="list-style-type: none"> – Short notice with only basic information about the issuer 	<ul style="list-style-type: none"> ▪ Issuer files Form D with SEC <ul style="list-style-type: none"> – Short notice with only basic information about the issuer
<ul style="list-style-type: none"> ▪ No limitation on investors (both accredited and non-accredited can purchase the offering) 	<ul style="list-style-type: none"> ▪ Unlimited number of accredited investors and up to 35 non-accredited investors
<ul style="list-style-type: none"> ▪ Investors receive restricted securities (resale restrictions) 	<ul style="list-style-type: none"> ▪ Investors receive restricted securities (resale restrictions)
	<ul style="list-style-type: none"> ▪ Under 506(c) general solicitation is permitted if offering is made only to accredited investors and the issuer takes reasonable steps to obtain written verification that the offering is made only to accredited investors

Sample Questions

Listed below are examples of questions which are relevant to the changes in Reg A and Reg D:

1. Based on the size of the issue, which of the following issuers could seek a registration exemption under Regulation A?
 - a. \$90 million aggregate offering of common stock, which includes \$22.5 million being sold on behalf of existing shareholders
 - b. \$100 million offering of newly issued common stock
 - c. \$75 million offering of newly issued common stock and a \$22.5 million sale on behalf of existing shareholders
 - d. \$75 million aggregate offering of common stock, which includes \$22.5 million being sold on behalf of existing shareholders

(D) Under the Regulation A exemption, the maximum size of an offering is \$75 million, with no more than \$22.5 million of the maximum offering being sold on behalf of existing shareholders. If the \$22.5 million that's sold on behalf of existing shareholders is in addition to the \$75,000,000 new shares being offered by the company, the exemption will NOT apply.

2. An issuer wants to raise capital in the U.S. and use both general solicitation and advertising to promote the offering. In addition, the issuer wants to avoid SEC registration and will not be selling to non-institutional investors. Which of the following offerings should be recommended to the issuer?
 - a. Regulation A offering
 - b. Regulation S offering
 - c. Regulation D 506(b) offering
 - d. Regulation D 506(c) offering

(D) Regulation D generally prohibits an issuer (or the securities firm that's representing the issuer) from using any form of general solicitation or advertising to promote an offering. However, under Rule 506(c), issuers and the firms that represent them may raise an unlimited amount of capital through the private placement market using general solicitation and advertising as long as all of the purchasers are accredited investors. Regulation S allows an issuer to raise capital outside the U.S. and avoid SEC registration by selling only to non-U.S. persons.

3. The limitation on the number of accredited investors that are permitted to purchase stock under a Regulation A offering is:
- 100
 - 99
 - Up to 35
 - There is no limitation.

(D) For a Regulation A offering, there's no limitation on the number of purchasers; instead, there's a dollar limitation of \$75 million. The limit of 35 non-accredited investors applies to private placements under Regulation D, not under Regulation A.

4. Which of the following statements is TRUE regarding a private placement of securities under Regulation D Rule 504?
- If the offering does NOT exceed \$10 million, the issuer is not required to file a Form D.
 - The offering can be made to both accredited and non-accredited investors.
 - The offering can exceed \$10 million if all of the investors are accredited.
 - If the offering does NOT exceed \$10 million, the antifraud provisions of the Securities Act of 1933 Act will NOT apply.

(B) Rule 504 of Regulation D allows an issuer to offer securities of up to \$10 million in a 12-month period to any investor (accredited and non-accredited). Provided the issuer complies with all of the provisions of Regulation D, this private placement is exempt from SEC registration. However, the issuer is still required to file Form D with the SEC by no later than 15 days after the first sale of securities. Under Regulation D Rule 504, the offering cannot exceed \$10,000,000. All offerings, regardless of whether they're exempt, are subject to the antifraud provisions of federal securities regulations.

5. An issuer can raise an unlimited amount of capital under which of the following?
- Regulation A Tier 1
 - Regulation A Tier 2
 - Regulation D Rule 504
 - Regulation D Rule 506

(D) Regulation D Rule 506 allows an issuer to raise an unlimited amount of capital from both accredited and up to 35 non-accredited investors. Regulation D Rule 504 limits the size of the offering to \$10 million, Regulation A Tier 1 has a maximum offering size of \$20 million, and Regulation A Tier 2 has a maximum offering size of \$75 million.

6. The use of general solicitation to offer securities for sale is NOT permitted in which of the following offerings?
- a. Regulation D Rule 506(b)
 - b. Regulation D Rule 506(c)
 - c. Regulation A Tier 1
 - d. Regulation A Tier 2

(A) An issuer conducting a private placement offering under Regulation D Rule 506 can raise an unlimited amount of capital without SEC registration. Rule 506(b) does NOT permit the use of general solicitation, but does allow for both accredited investors and up to 35 non-accredited investors. Rule 506(c) permits the use of general solicitation as long as all of the investors are accredited and reasonable steps are taken to obtain written verification that the offering is made only to accredited investors. Under Regulation A, general solicitation is permitted for both Tier 1 offerings (up to \$20 million) and Tier 2 offerings (up to \$75 million). Regulation A also allows the offering to be made to any type of investor.