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SEC Proposes Increased Thresholds for Exchange Act Registration Pursuant to the JOBS Act

In December 2014, the SEC proposed rules under the Jumpstart Our Business Startups Act (the "JOBS Act") that reflect new, higher thresholds for registration under the Securities Exchange Act of 1934 (the "Exchange Act"). The SEC also proposed rules that would implement higher thresholds for termination of registration and suspension of reporting for banks and bank holding companies and savings and loan holding companies. In addition, the SEC has proposed to revise the definition of "held of record" in Exchange Act Rule 12g5-1 to exclude certain securities held by persons who received them pursuant to employee compensation plans and to establish a non-exclusive safe harbor for determining whether securities are "held of record" for purposes of registration under Exchange Act Section 12(g).

Background

The JOBS Act amended Sections 12(g) and 15(d) of the Exchange Act to adjust the thresholds for registration, termination of registration and suspension of reporting. Specifically, the JOBS Act amended Section 12(g)(1) of the Exchange Act to require an issuer to register a class of equity securities (other than exempted securities) within 120 days after its fiscal year end if, on the last day of its fiscal year, the issuer has total assets of more than $10 million and a class of equity securities is "held of record" by either (i) 2,000 persons, or (ii) 500 persons who are not accredited investors. The prior threshold had been 500 record holders without regard to accredited investor status.

The JOBS Act established a separate registration threshold for banks and bank holding companies and savings and loan holding companies pursuant to which an issuer must register a class of equity securities (other than exempted securities) within 120 days after the last day of its fiscal year end if, on the last day of its fiscal year, the issuer has total assets of more than $10 million and the class of equity securities is "held of record" by 2,000 or more persons, without regard to accredited investor status. The JOBS Act also amended the Exchange Act to enable an issuer that is a bank, a bank holding company or a savings and loan holding company to terminate the registration of a class of securities under Section 12(g) or suspend reporting under Section 15(d)(1) if that class is held of record by less than 1,200 persons. For other issuers, the threshold for termination of registration and suspension of reporting remains at 300 persons.

The JOBS Act also amended the Exchange Act to exclude from the definition of "held of record," for purposes of determining whether an issuer is required to register a class of equity securities, securities

that are held by persons who received them pursuant to an "employee compensation plan" in transactions exempted from the registration requirements of Section 5 of the Securities Act.

The Proposed Rules

Increased Thresholds for Registration and Reporting Requirements

The SEC has proposed amendments to Rule 12g-1 under the Exchange Act that would exempt an issuer from the requirement to register a class of equity securities and comply with reporting obligations under the Exchange Act if the class of equity securities was held of record by fewer than 2,000 persons or 500 persons who are not accredited investors. The SEC is not proposing to establish a new definition of "accredited investor" for purposes of the new rule and would rely on the existing definition of "accredited investor" contained in Securities Act Rule 501(a). The "accredited investor" determination would be made as of the last day of the fiscal year rather than at the time of the sale of the securities.

The proposed rules establish a separate threshold for banks and bank holding companies and savings and loan holding companies that would exempt an issuer from the registration and reporting requirements of the Exchange Act if the class of equity securities was held by fewer than 2,000 persons, without regard to accredited investor status.

Amendments to Termination and Suspension Requirements for Banks and Bank Holding Companies and Savings and Loan Holding Companies

The SEC is proposing changes to the thresholds contained in Rules 12g-2 and 12g-3 under the Exchange Act for terminating registration and suspending reporting requirements applicable to banks and bank holding companies and savings and loan holding companies from 300 persons to 1,200 persons. Rules 12g-4 and 12h-3 currently permit issuers, once reaching the designated threshold, to immediately suspend their duty to file periodic and currently reports. The proposed rule changes would allow banks and bank holding companies and savings and loan holding companies to rely on the SEC's rules to suspend reporting immediately, to avoid being deemed registered upon the termination of certain exemptions or as a successor issuer, and to terminate their registration during the fiscal year, at the higher 1,200-holder threshold. This higher threshold was established in order to accommodate concerns of smaller community banks.

Exclusion from Definition of "Held of Record" of Securities Received Pursuant to Employee Compensation Plan

The JOBS Act provides that the definition of "held of record" shall not include securities held by persons who received them pursuant to an "employee compensation plan" in transactions exempted from the

registration requirements of Section 5 of the Securities Act. The term "employee compensation plan" is not defined.

Rather than creating a new definition for the term "employee compensation plan," the SEC is proposing to revise the definition of "held of record" and to establish a non-exclusive safe harbor that relies on the current definition of "compensatory benefit plan" in Rule 701 and the conditions in Rule 701(c). The SEC believes that by not defining the term "employee compensation plan," and by providing for a non-exclusive safe harbor, it is providing issuers with flexibility in their determinations under Section 12(g)(5).

Held of Record. The SEC is proposing to amend the definition of "held of record" to provide that when determining whether an issuer is required to register a class of equity securities with the SEC pursuant to Exchange Act Section 12(g)(1) an issuer may exclude securities that are either:

- held by persons who received the securities pursuant to an employee compensation plan in transactions exempt from the registration requirements of Section 5 of the Securities Act or that did not involve a sale within the meaning of Section 2(a)(3) of the Securities Act (these latter issuances being so-called "no sale" issuances); or

- held by persons eligible to receive securities from the issuer pursuant to Exchange Act Rule 701(c) who received the securities in a transaction exempt from the registration requirements of Section 5 of the Securities Act in exchange for securities excludable under proposed Rule 12g5-1(a)(7). This exclusion is intended to facilitate the ability of issuers to conduct restructurings, business combinations and similar transactions that are exempt from Securities Act registration so that if the securities being surrendered would not have counted as "held of record" the securities issued in exchange also would not count. Securities held of record by former employees would be excluded only if the employees were employed by or providing services to the surviving issuer at the time the exchange securities were offered.

*Non-exclusive Safe Harbor for Determining Holders of Record***.** The SEC proposes that an issuer would be able to rely on the safe harbor for determining the holders of securities issued in reliance on Securities Act Rule 701, as well as holders of securities issued in transactions otherwise exempted from, or not subject to, the registration requirements of the Securities Act that satisfy the conditions of Rule 701(c), even if all the other conditions of Rule 701, such as issuer eligibility in Rule 701(b)(1), the volume limitations in Rule 701(d) or the disclosure delivery provisions in Rule 701(e), were not met.

Thus, the safe harbor would be available for holders of securities received in other employee compensation plan transactions exempted from, or not subject to, the registration requirements of Section 5 of the Securities Act, such as securities issued in reliance on Securities Act Section 4(a)(2), Regulation D of the Securities Act, or Regulation S of the Securities Act, that meet the conditions of Rule

701(c). Note that once the securities are transferred, the securities would need to counted as held of record by the transferee for purposes of the Section 12(g)(1) calculation.

In addition, under the proposed rules, foreign private issuers would be able to rely on the safe harbor when making their determination of the number of U.S. resident holders under Exchange Act Rule 12g3-2(a). Under Rule 12g3-2(a), foreign private issuers that meet the asset and shareholder thresholds of Section 12(g) are exempt from registering any class of securities under that section if the class of securities is held by fewer than 300 holders resident in the United States. For purposes of determining whether this threshold is met, Rule 12g3-2(a)(1) specifies that the method shall be as provided in Exchange Act Rule 12g5-1, subject to specific provisions relating to brokers, dealers, banks and nominees. Because the rule directs issuers to the definition of "held of record" in Rule 12g5-1, the statutory changes to Section 12(g)(5) as well as the proposed changes to Rule 12g5-1 would also apply to the determination of a foreign private issuer's U.S. resident holders for the purposes of the Rule 12g3-2(a) analysis. Note that securities held by employees are to continue to be counted for purposes of determining the percentage of the issuer's outstanding securities held by U.S. residents and foreign private issuer status.

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The SEC will continue to solicit comments on the proposed rules discussed above until 60 days following their publication in the federal register. For a copy of the proposed rules and the SEC's accompanying release, see: http://www.sec.gov/rules/proposed/2014/33-9693.pdf

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This memorandum is not intended to provide legal advice, and no legal or business decision should be based on its content. Questions concerning issues addressed in this memorandum should be directed to:

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