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Via Electronic Submission

June 26, 2013

U.S. Securities and Exchange Commission
100 F Street NE
Washington, DC 20549-1090

Re: Request for Public Comments on SEC Regulatory Initiatives under the JOBS Act Relating to Section 12(g) of the Securities Exchange Act of 1934, as amended by JOBS Act Title V- Private Company Flexibility and Growth, Title VI – Capital Expansion, and Title III – Crowdfunding

Ladies and Gentlemen:

This letter is submitted on behalf of the Federal Regulation of Securities Committee (the "Committee") of the Business Law Section (the "Section") of the American Bar Association (the "ABA") with respect to the rules the Securities and Exchange Commission (the "Commission") is required to adopt pursuant to the Jumpstart Our Business Startups Act of 2012 (the "JOBS Act"). This letter is submitted in response to the Commission's request for public comments relating to the JOBS Act rulemaking.[1]

The comments outlined in this letter represent the views of the Committee, and have also been prepared in conjunction with, and reviewed and approved by, the Middle Market and Small Business Committee, the Private Equity and Venture Capital Committee, and the State Regulation of Securities Committee of the Section. The comments expressed in this letter have not been approved by the ABA's House of Delegates or Board of Governors and therefore do not represent the official position of the ABA. In addition, these comments do not represent the official position of the Section.

The Committee thanks the Commission for this opportunity to comment on the JOBS Act provisions set forth in Titles V and VI, and Section 303 of Title III, relating to registration of a class of securities under Section 12(g) of the Securities Exchange Act of 1934, as amended ("Exchange Act"). Because this letter is being submitted prior to the Commission's issuance of proposed rules, our comments are intended to highlight matters we believe the Commission should consider in formulating its proposed rules pursuant to Titles III, V and VI, or in providing guidance with respect thereto.

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1 http://www.sec.gov/spotlight/jobsactcomments.shtml.

Summary of Our Comments

Our comments with respect to Titles III, V and VI of the JOBS Act, which, among other things, amend Section 12(g) of the Exchange Act, are as follows:

A. Defining the Term "Accredited Investor" for Purposes of Section 501 of Title V

1. The Commission should confirm that the definition of "accredited investor" is the same as the definition codified in Rule 501(a) of Regulation D under the Securities Act of 1933, as amended ("Securities Act").

2. The Commission's Title V rules should not require issuers, as a condition to concluding that a shareholder is (or is not) an "accredited investor", to take reasonable steps to verify such status.

3. The Commission should provide guidance regarding the type of information upon which issuers may rely in determining a record holder's accredited investor status.

   a) The issuer should be permitted to rely on determinations of "accredited investor" status made by specified categories of third parties, including financial and other intermediaries.

   b) The issuer should be permitted to rely on a certification by the investor and on other information obtained by the issuer.

   c) Issuers should be permitted to rely on an annual affirmation from investors that their information or status as accredited investors has not changed from prior years. If an investor fails to respond to the annual inquiry in any year, the issuer should be entitled to rely on information from prior years, in the absence of any information of which an executive officer of the issuer is aware that would lead the issuer reasonably to believe that the information from prior years was unreliable or has changed.

   d) Issuers should be permitted to make determinations concerning an investor's "accredited investor" status during a reasonable period before or after the fiscal year-end, without having to make a separate judgment precisely as of the end of the fiscal year in question.

B. The Employee Compensation Plan Securities Carve-out From the "Held of Record" Definition Under Exchange Act Section 12(g)(5)

1. The employee compensation plan securities safe harbor rule(s) should be a non-exclusive means of complying with Section 12(g)(5), as amended by Title V of the JOBS Act.

2. The safe harbor rules should encompass transactions that are exempt under any exemption or exemptive safe harbor from, or otherwise not subject to, registration under Securities Act Section 5.

3. The definition of "employee compensation plan" under the safe harbor rule(s) should encompass all transactions covered by Securities Act Rule 701(c), and should cover securities acquired by family members from employees (or former employees) and upon the employee's (or former employee's) death (or disability) pursuant to a non-sale transaction.

4. The provision of financial statements to employees, former employees and other covered persons should not be a condition to reliance on the new Section 12(g)(5) safe harbor rule(s).

5. The safe harbor rule(s) should provide that, in the event of a subsequent transaction (including a business combination) that is exempt from, or otherwise is not subject to, the registration requirements of Section 5, the securities issued in that transaction to eligible employees and other covered persons in exchange for securities covered by the Section 12(g)(5) compensatory plan securities carve-out (including any Commission safe harbor rule thereunder) also are covered by the Section 12(g)(5) carve-out.

6. The safe harbor rule(s) should provide that the Section 12(g)(5) carve-out is not affected by the form in which the compensatory plan securities are held by employees, former employees or permitted transferees.

7. If a broad safe harbor rule (or rules) is adopted under Section 12(g)(5), Exchange Act Rule 12h-1(f) will no longer be necessary, but Rule 12h-1(g) may have continuing application.

8. The Commission should adopt a safe harbor rule that enables companies with a class of equity securities registered under Section 12(g) of the Exchange Act, or that are reporting under Section 15(d) of the Exchange Act, to return to private company status if they have fewer than 300 holders of record after applying the Section 12(g)(5) carve-out for compensatory plan securities.

9. Issuers should be able to make determinations concerning an equity holder's status for purposes of the Section 12(g)(5) carve-out (i.e. as an eligible employee, former employee or other covered person) during a reasonable period before or after the fiscal year-end, without having to make a separate determination as of the end of the fiscal year in question.

10. The Section 12(g)(5) carve-out for employee compensatory plan securities, and any safe harbor(s) or other Commission rule implementing that carve-out, should apply to the determination by a bank or bank holding company of the number of record holders under Section 12(g)(1)(B), as amended by Section 601 of Title VI of the JOBS Act.

C. The Crowdfunding Exemption Under Exchange Act Section 12(g)(6)

1. The Commission should confirm that the Exchange Act Section 12(g)(6) exemption applies to, and flows with, the securities initially acquired in a crowdfunding offering, and that the exemption therefore is not limited to the securities in the hands of the initial purchaser in that offering.

2. The rule should provide that the Section 12(g)(6) exemption survives and attaches to securities issued in a subsequent restructuring, recapitalization or similar transaction that is exempt from, or otherwise not subject to, the registration requirements of Section 5, so long as the parties to the subsequent transaction are affiliates of the original issuer.

3. The availability of the exemption set forth in Exchange Act Section 12(g)(6), and/or any exemptive safe harbor adopted thereunder by the Commission, should be conditioned on: (a) issuance of the securities in question in a transaction that qualifies for the Securities Act Section 4(6) exemption; or (b) the issuer's reasonable belief, at the time of the annual Section 12(g) determination, that the Section 4(6) exemption (and/or an exemptive safe harbor thereunder) was available in connection with the original crowdfunding transaction. But only post-transaction obligations that are within the issuer's control should be considered in determining whether the exemption's conditions were met.

4. The availability of the exemption under Section 12(g)(6) and/or any exemptive safe harbor adopted thereunder by the Commission, should be conditioned on the issuer not having total assets, as of the last day of the fiscal year with respect to which the Section 12(g) compliance determination is made (or a reasonable period before or after such date), in excess of $25 million.

5. The Commission should extend any Section 12(g)(6) exemptive safe harbor treatment to eligible banks and bank holding companies that engage in exempt crowdfunding offerings under Section 4(6) of the Securities Act.

Background

As amended by Title V of the JOBS Act, Exchange Act Section 12(g) now requires registration if, at the end of its fiscal year, a company has at least $10 million in assets and a class of equity securities held of record by either (i) 2,000 persons, or (ii) 500 persons who are not accredited investors. Under Title VI, banks and bank holding companies are not required to register unless they have, at the end of the fiscal year, at least $10 million in assets and a class of equity securities held of record by 2,000 or more persons. Commission rulemaking relating to Exchange Act Section 12(g) registration is required under Titles III, V and VI, although the Commission's staff has indicated that the employee compensation plan securities holder carve-out from the definition of "held of record" set forth in Section 502 (amending Exchange Act Section 12(g)(5)) became effective for both non-bank issuers and bank holding companies on the date of enactment of the JOBS Act, April 5, 2012.[2]

Under Title V of the JOBS Act, Exchange Act Section 12(g)(5) has been amended to provide that the term "held of record" does not include "securities held by persons who received the securities pursuant to an employee compensation plan in transactions exempted from the registration requirements of section 5 of the Securities Act." The Commission is directed by Section 503 of the JOBS Act to: (1) amend its Rule 12g5-1 definition of the term "held of record" to reflect this amendment to the statute; and (2) adopt "safe harbor provisions" for issuers to follow in determining whether holders of their securities received those securities pursuant to "an employee compensation plan in transactions that were exempt from the registration requirements of section 5 of the Securities Act of 1933". In addition, Section 303 of Title III of the JOBS Act directs the Commission to, "by rule, exempt, conditionally or unconditionally, securities acquired pursuant to an offering made under section 4(6) of the Securities Act [*i.e.* an exempt crowdfunding offering] from" registration under Exchange Act Section 12(g).

The purpose of this comment letter is to assist the Commission in connection with its formulation of proposed rulemaking and/or guidance to implement the Section 12(g)-related amendments effected by certain provisions of JOBS Act Titles III, V and VI.

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2 Question 5, FAQs on Titles V and VI of the JOBS Act (April 11, 2012), available at http://www.sec.gov/divisions/corpfin/guidance/cfjjobsactfaq-12g.htm.

Discussion

A. Defining the Term "Accredited Investor" for Purposes of Section 501 of Title V

1. The Commission should confirm that the definition of "accredited investor" is the same as the definition codified in Rule 501(a) of Regulation D under the Securities Act.

Section 501 of the JOBS Act does not define the term "accredited investor", but instead refers to "accredited investors (as such term is defined by the Commission)". In our view, it is reasonable to conclude that Congress intended the term "accredited investor" in Section 501 to refer to the definition of "accredited investor" as set forth in Rule 501(a) of Regulation D under the Securities Act. In the Report on Authority to Enforce Exchange Act Rule 12g5-1 and Subsection (b)(3)[3], which was mandated by Section 504 of the JOBS Act, the Commission staff appears also to have taken this position. Specifically, in footnote 4 of the Report, the Commission staff cited to Rule 501 of Regulation D in its discussion regarding the JOBS Act amendments to Section 12(g). We concur with this view, and believe that any other definition would be inconsistent with Congressional intent and would create needless complexity and impose unnecessary costs on issuers. We therefore suggest that the Commission's proposed rule or rulemaking release clearly state that the Rule 501(a) definition of "accredited investor" is the definition applicable to the Commission's rulemaking under Section 501 of the JOBS Act.

The Securities Act Rule 501(a) definition of "accredited investor" includes both persons (and entities) who meet the objective standards set forth in any of the eight categories of Rule 501(a), and persons (and entities) whom the issuer reasonably believes fall within any of these categories. This bifurcated definition thus serves the important purpose of enabling an issuer reasonably to rely on credible information available to it bearing on a particular investor's eligibility, even if that information proves ultimately to be incorrect. In our view, the reasonable belief standard currently included in the Rule 501(a) definition should apply to determinations of "accredited" investor status for purposes of Section 12(g)(1)(A)(ii) of the Exchange Act.

2. The Commission's Title V rules should not require issuers, as a condition to concluding that a shareholder is (or is not) an "accredited investor", to take reasonable steps to verify such status.

Although Section 201(a) of the JOBS Act requires issuers engaged in a Rule 506 transaction using general solicitation or general advertising to limit purchasers to accredited investors, and to take reasonable steps to verify that purchasers of the securities are accredited investors, using such methods as the Commission may determine, we do not believe these same standards should apply to the Title V "holder of record" determination. We recognize that issuers with more than 500 holders of record of a class of equity securities that seek to avoid Section 12(g) registration are required to determine, as of the last day of any fiscal year, whether

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[3] Report on Authority to Enforce Exchange Act Rule 12g5-1 and Subsection (b)(3) (October 15, 2012) (the "Report"), available at http://www.sec.gov/news/studies/2012/authority-to-enforce-rule-12g5-1.pdf.

their equity holder base includes a number of accredited investors at least as great as the difference between the total number of holders of record of a given class of equity securities that must be counted for Section 12(g) purposes and 500. However, these determinations will be very different from judgments made by the issuer or its agent in the context of deciding whether securities in a Rule 506 offering accompanied by general solicitation and/or advertising can be sold to any particular offeree. Moreover, the Commission has proposed to leave intact – in proposed Securities Act Rule 506(b) – an issuer's ability to conduct a "quiet" private placement that would not require "reasonable steps to verify" a purchaser's accredited investor status as a condition to reliance on this particular prong of the Securities Act Rule 506 exemptive safe harbor.

In any case, as noted, the annual Section 12(g)(1) record holder determination generally will be made outside of the context of a particular exempt private offering by the issuer, and may involve investors (such as heirs or other transferees of the initial investor in an exempt private offering) with whom the issuer has had little or no prior contact. These investors may be difficult to contact and may be reluctant to provide personal financial information to the issuer under circumstances that do not involve an investment decision (either by the initial purchaser from the issuer or by a buyer in a subsequent resale transaction).

We believe the Commission should take cognizance of the burden that any verification obligation would impose on companies seeking to avail themselves of the additional flexibility provided by Section 501 of the JOBS Act, particularly those smaller non-reporting companies that have not yet decided whether to conduct an IPO. The type of information available to an issuer, and the issuer's ability to obtain additional information from its investors, will vary greatly depending on the particular facts and circumstances. We believe that issuers should have the discretion to make reasonable judgments about the reliability of the information available to them in assessing the "accredited investor" status of record holders for Section 12(g)(1) registration purposes, without being required to take the same measures to verify such information that otherwise would be appropriate in a Securities Act transactional context.

3. *The Commission should provide guidance regarding the type of information upon which issuers may rely in determining a record holder's accredited investor status*.

While some issuers may prefer the certainty that compliance with the conditions to a safe harbor would provide, others may seek flexibility to make reasonable judgments concerning a shareholder's status as an accredited investor. Similar to the Commission's approach in the General Solicitation Release,[4] it would be helpful if the Commission were to provide guidance regarding the type of information upon which issuers may rely in determining a record holder's accredited investor status. The following is a non-exclusive list of the types of information that we would urge the Commission to consider proposing for public comment:

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4 Release No. 33-9354, "*Eliminating the Prohibition Against General Solicitation and General Advertising in Rule 506 and Rule 144A Offerings*" (August 29, 2012), available at http://www.sec.gov/rules/proposed/2012/33-9354.pdf

a. *The issuer should be permitted to rely on determinations of "accredited investor" status of a record holder made by specified categories of third parties, including financial and other intermediaries*.

Issuers should be able to rely on determinations of a record holder's "accredited investor" status made by third parties. As the Commission stated in the General Solicitation Release, third parties that provide reasonably reliable evidence of a holder's accredited investor status can provide a reasonable basis for the issuer's determination. For example, registered broker-dealers may collect and verify information as to a person's status as an "accredited investor" in connection with resales of securities conducted in reliance on the so-called Securities Act "Section 4(a)(1-1/2)" exemption. Absent transfer restrictions requiring the consent of the issuer, the information collected by a broker-dealer or other intermediary may be the issuer's only source of data regarding an investor who acquired securities in a particular resale transaction. Such an intermediary also may be the entity charged with collecting investor eligibility information in a primary exempt offering by the issuer. In addition, in the future it is possible that some intermediaries will offer accredited investor verification services as a separate service available both to issuers and investors (e.g., in a resale context), similar to what now exists in connection with Securities Act Rule 144A resale transactions.[5] The intermediaries may be better equipped to perform this function in some situations, and may be able to collect and retain data more efficiently and at less cost than issuers.

For privacy reasons, or to eliminate the need for multiple certifications to different issuers, investors themselves may prefer to provide sensitive personal financial information to a single third party intermediary, rather than providing that information directly to the issuer. Accordingly, we believe it would be appropriate for the Commission to allow issuers to rely on determinations of accredited investor status made by a specified type of third party intermediary. In many cases the intermediary may be a regulated financial institution such as a bank, or a broker-dealer or investment adviser that is registered with the Commission. Lawyers and accountants also might perform the same service.

b. *The issuer should be permitted to rely on a certification by the investor and on other information obtained by the issuer*.

In private exempt offerings, it is common for an issuer to rely on representations from the investor regarding his or her (or its) "accredited investor" status, whether in the form of responses to an investor questionnaire and/or execution of a subscription agreement containing buyer representations and warranties. Such a certification should be deemed sufficient in the context of Section 12(g)(1)(A)(ii) in the absence of any "red flag" putting the issuer on notice that this information is unreliable.

In lieu of investor questionnaires, an issuer may also be able to obtain information from other sources. For example, issuers would be able to ascertain that certain employees have

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5 *See* Communicator Inc. (Sept. 19, 2002).

sufficient income to meet the annual income test for individual accredited investors (although we believe issuers would prefer in this context to rely on the compensatory plan carve-out set forth in Exchange Act Section 12(g)(5), as discussed below in Part B). For investors that are entities, there may be sufficient information available publicly to determine that the entity is an accredited investor. In addition, information from a variety of sources may bear on whether information submitted by an investor is or continues to be reliable. Even in the absence of the receipt of information directly from the holders of record, issuers should be able to take cognizance of any relevant information in forming a reasonable belief that an investor is accredited (including the market value of the holder's position in the issuer's securities), just as the issuer would need to consider any red flags that might indicate that an investor is not accredited.[6]

In an analogous context, a seller of securities under Rule 144A under the Securities Act is permitted to rely on several possible, nonexclusive methods for forming a reasonable belief that the prospective purchaser is a qualified institutional buyer. Pursuant to Rule 144A(d), a seller may rely on, among other things, the prospective purchaser's publicly available financial statements, information provided to U.S. or foreign regulatory agencies, or a certification of the purchaser's chief financial officer. Issuers should be allowed to rely on similar sources of information in determining whether a shareholder is an accredited investor for purposes of Exchange Act Section 12(g)(1).

c. *Issuers should be permitted to rely on an annual affirmation from investors that their information or status as accredited investors has not changed from prior years. If an investor fails to respond to the annual inquiry in any year, the issuer should be entitled to rely on information from prior years, in the absence of any information of which an executive officer of the issuer is aware that would lead the issuer reasonably to believe that the information from prior years was unreliable or has changed*.

Section 12(g)(1)(A)(ii) requires issuers to make an annual determination as to whether they will be required to register a class of equity securities because of the number of non-accredited investor holders of record. In counting the number of accredited investors, issuers may wish to rely on information that is more than one year old as to the accredited status of certain investors and, in many cases, it may be appropriate to do so. In other situations it may be more prudent to inquire on an annual basis as to the accredited status of each investor. Investors could either supply new information or confirm that specific information about their income, net worth or assets already provided had not changed. Of course, the investor response rate to any communication from the issuer, annual or otherwise, is unlikely to be 100%. In the absence of a response from the investor in any particular year, the issuer thus should be permitted to assume

6 The ability to rely on a variety of different sources of information available to the issuer was proposed in the Commission's General Solicitation Release, *supra* note 4.

that the information has not changed since the date of original investment or resale, as the case may be (or a subsequent update by the investor obtained in prior years), unless an executive officer of the issuer has reason to believe that the information has changed in a way that would result in the loss of accredited investor status. For example, an investor whose net worth was credibly shown to be significantly above the $1 million amount in one year might be assumed to meet the net worth test in the succeeding years, in the absence of a response from the investor in the next year, or other information indicating that this assumption is unreasonable.

While issuers in the future may wish to include contractual covenants or provisions in corporate governance documents requiring equity holders to respond to requests from the issuer to verify their accredited investor status, not all will do so and existing investors may not be under any such obligation. It is likely, moreover, that some investors will not respond even if they are required to do so. Allowing issuers to rely on a prior year's information or other information available to the issuer, as outlined above, will therefore be helpful to the smaller companies that the JOBS Act is designed to assist.

d. *Issuers should be permitted to make determinations concerning an investor's "accredited" status during a reasonable period before or after the fiscal year-end, without having to make a separate judgment precisely as of the end of the fiscal year in question.*

Although Section 501 of the JOBS Act requires issuers to determine the number of unaccredited record holders of a class of equity securities as of the end of a given fiscal year, we believe that issuers should have some flexibility on the timing of that determination. In other words, the Commission should permit issuers to make the judgment about which equity holders are accredited investors and which are not, during a reasonable period of time before or after the end of the year, based on information available to them at the time they make their judgment. For example, a calendar year issuer might wish to make inquiries of its investors several months in advance of the fiscal year-end, in order to determine whether it needed to register under Section 12(g) in the following year. In other cases, an issuer may not become aware of the need to obtain information concerning transferee investors until after the end of its fiscal year. Issuers should be able to rely on information furnished during these times, whether by an investor or an intermediary, without having to update the information as of the end of the fiscal year. As described above, there will also be many times when information provided in prior years will continue to be relevant and reliable, and issuers should be able to rely on such older information when it is not unreasonable to do so.

B. The Employee Compensation Plan Securities Carve-out from the "Held of Record" Definition under Exchange Act Section 12(g)(5)

Section 502 of the JOBS Act amends Section 12(g)(5) of the Exchange Act to provide that, for purposes of determining whether an issuer is required to register a class of equity securities under Section 12(g), "the definition of 'held of record' shall not include securities held by persons who received the securities pursuant to an employee compensation plan in transactions exempted from the registration requirements of section 5 of the Securities Act of

1933." Section 503 of the JOBS Act directs the Commission both to revise the definition of "held of record" to implement amended Section 12(g)(5)'s "carve-out", and in addition to "adopt 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 the registration requirements of [Securities Act] Section 5…."

We believe that the policy objectives underlying these provisions reflect a legislative understanding that equity securities issued under employee compensatory plans of smaller private companies should be treated differently for purposes of registration under Section 12(g), to permit the issuance of equity securities under such plans to compensate employees without forcing these companies to register a class of securities under Section 12(g) before they are prepared to shoulder the costs and other burdens associated with becoming a public company.

Although the benefits of amended Section 12(g)(5) have been available to issuers since the date of enactment of the JOBS Act, we believe that many smaller private companies are unlikely to take advantage of the new compensatory plan securities "carve-out" from the calculation of record holders codified in Section 12(g)(5) absent Commission implementation of its Section 503 rulemaking obligations (as described above). In addition, we believe that the safe harbor rule (or rules) adopted by the Commission should be sufficiently broad to enable companies to rely on it (or them) without undue concern that their employee compensation programs will inadvertently trigger Exchange Act registration.

1. *The employee compensation plan securities safe harbor rule(s) should be a non-exclusive means of complying with Section 12(g)(5), as amended by Title V of the JOBS Act.*

We believe that the safe harbor rule(s) proposed by the Commission in accordance with Section 503 of the JOBS Act should expressly provide that the safe harbor(s) is <u>not</u> the exclusive means by which an issuer may comply with the "compensatory plan carve-out" provisions of Section 12(g)(5). By mandating that regulatory safe-harbor provisions be adopted in addition to the statutory carve-out, we believe that the text of Section 503 itself indicates a legislative intent that failure to satisfy all conditions to reliance on the safe harbor(s) should not preclude reliance on the statutory carve-out itself.

The Commission should confirm that issuers may rely on the statutory carve-out alone both before and after adoption of the new safe harbor rule(s). The Division of Corporation Finance has taken this position with respect to reliance on the statutory provision before adoption of the safe harbor rule (or rules),[7] and the same principle logically should extend to reliance after adoption of the safe harbor rule(s). Such an approach also would be consistent with that taken by the Commission in connection with safe harbor rules promulgated under the Securities Act, such as Rules 144 and 506, both of which were expressly designated as non-exclusive safe harbors – thus allowing the seller to rely in the alternative on the underlying statutory exemption should it fail to meet all of the express conditions to reliance on the safe harbor. Because Congress has opted to import Securities Act concepts into the Exchange Act via various JOBS Act

[7] *See* Question 5 of the JOBS Act FAQs, *supra* note 2.

amendments, it follows that the important Securities Act concept of non-exclusivity should be reflected in the new Section 12(g) safe harbor rules.

2. *The safe harbor rules should encompass transactions that are exempt under any exemption or exemptive safe harbor from, or otherwise not subject to, registration under Securities Act Section 5.*

We believe the Commission's safe harbor rules should cover equity securities received by employees (and other covered persons, as discussed below) pursuant to compensatory plans, regardless of which exemption from Securities Act registration was utilized in connection with their issuance. The plain language of the statutory mandate for the safe harbor is broad, on its face encompassing all exemptions from Securities Act registration. Borrowing from Rule 701 for the purpose of defining the term "written compensatory plan", which we recommend in the next subsection of this letter, should not be a reason to limit the safe harbor rule(s) to equity securities offered under the Rule 701 exemption.

The new Section 12(g)(5) safe harbor(s) should account for the fact that various exemptions other than Rule 701 are regularly utilized by companies for their compensatory programs. In particular, companies may use Regulation S when issuing securities to foreign employees; Section 3(a)(2) for company contributions to 401(k) and other tax-qualified plans; Rule 506 and Section 4(a)(2) when issuing compensatory securities in excess of the Rule 701 limits to accredited investors; and Rule 504 (when the Rule 701 limits are exceeded by only a small amount). Though now used infrequently, Regulation A may be invoked more often by issuers of compensatory plan securities once the Commission raises the $5 million ceiling to $50 million pursuant to the Title IV JOBS Act amendments to Securities Act Section 3(b). Accordingly, the language of the safe harbor(s) should be broad enough to cover this and any other Section 5 exemptive provisions that the Commission might adopt in the future.

In addition, we believe that the safe harbor rule(s) should expressly provide that securities issued in unregistered transactions based on the "no-sale" doctrine developed by the Commission and its staff under Securities Act Section 2(a)(3), are included within the definition of "transactions exempt from Section 5."

We believe it is important that securities issued to employees and other covered persons under compensatory plans be excluded – at the issuer's option – from the record holder count for purposes of Section 12(g) under the employee plans safe harbor(s), even if a particular holder received the compensatory plan securities under an exemption for "accredited investors". In many cases, recipients of equity securities under compensatory plans qualify as accredited investors because of their positions as executive officers or directors, but will no longer qualify as such once their employment or directorship with the company terminates (unless they independently meet the annual income/net worth tests). Yet if other former employees are excluded from the count of holders of record for purposes of Section 12(g), which we strongly believe should be the case, former officers and directors should *a fortiori* be excluded from the count, regardless of the exemption from Securities Act registration under which their compensatory shares were issued.

We also note and agree with the statement by Senator Toomey, who authored an earlier bill containing the compensatory plan exemption, that the safe harbor rule should provide issuers with greater certainty that the compensatory plan exemption is available by enabling an issuer to treat an issuance of securities as exempt from Securities Act registration for purposes of Section 12(g)(5) if that issuer has a reasonable belief that the exemption was available at the time the securities were issued.[8]

3. *The definition of "employee compensation plan" under the safe harbor rule(s) should encompass all transactions covered by Securities Act Rule 701(c), and should cover securities acquired by family members from employees (or former employees) and upon the employee's (or former employee's) death (or disability) pursuant to a non-sale transaction.*

We recommend that the Commission incorporate into the definition of "employee compensation plan" under the safe harbor rule(s) the full range of compensatory arrangements and security holders described in Rule 701(c) under the Securities Act. In particular, we believe it is important that the concept of "employee compensation plan" encompass both traditional plans and individual compensatory agreements and include compensatory arrangements established by the various entities related to the issuer enumerated in Rule 701(c). Moreover, we believe this concept also should cover equity securities in the hands of the full range of participants and permitted transferees enumerated in Rule 701(c) – including not only employees, officers, directors, consultants and other direct service providers (collectively referred to as "employees" in this letter), but also former employees and family members (as defined in Rule 701(c)(3)) who acquired the securities from employees (and former employees) through gifts or domestic relations orders. Although we believe that Rule 701(c) extends to family members who acquire compensatory plan securities from an employee (or former employee) by gift or domestic relations order, or upon an employee's (or former employee's) death (or disability), as well as to the executor or guardian of the employee, former employee, or family member who acquires the securities upon such person's death or disability, we recommend that the Commission explicitly import this interpretation of Rule 701(c) into the proposed safe harbor under Exchange Act Section 12(g)(5) to avoid any confusion.

We believe that including as permitted transferees family members who receive the securities by virtue of the employee's (or former employee's) gift, domestic relations order, death, or disability is necessary to avoid inadvertent loss of the compensatory plan carve-out as a result of such transfers. Because such transfers are outside the control of the issuer, the possible loss of the compensatory plan carve-out over time due to such transfers would create substantial uncertainty for issuers in determining whether and when the Section 12(g) registration requirements would be triggered. Such uncertainty might lead the issuer to limit its use of equity compensation, contrary to the intent of Congress as expressed in the JOBS Act. Moreover, we believe that family members who receive compensatory securities in a non-sale transaction upon

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[8] *See* statement of Senator Toomey in the Congressional Record, 112th Congress, page S2230 (March 29, 2012).

the employee's (or former employee's) death or disability should not be treated differently from those who receive them as a gift during the employee's (or former employee's) lifetime. Similarly, the status of the donee for purposes of the compensatory plan carve-out should not be affected by whether the gift or other non-sale transfer of compensatory equity securities occurred during or after the employee's employment by the issuer, so long as the donor/transferor originally received the securities when employed by or otherwise serving the issuer in a capacity covered by Rule 701(c).

We recognize that the Commission has a number of different regulatory templates to draw from in proposing rules under the Section 503 mandate, including Securities Act Rule 405 (definition of "employee benefit plan"), Rule 701, Regulation S-K Item 402(a)(6)(ii), and Exchange Act Rules 12h-1(f) and (g). From the perspective of most start-up private companies, however, application in a Section 12(g) context of the familiar concepts applied in connection with the exempt issuance of compensatory equity securities under Rule 701 will facilitate compliance by streamlining a smaller issuer's learning curve and simplifying recordkeeping. This result is entirely consistent with Congress' clear intent to make it easier for smaller companies to remain private for an extended period, if they so choose.

We note that Rule 701(c) calls for a written compensatory arrangement. We believe that the requirement of a written arrangement is reasonable in the Section 12(g)(5) context, as well as for Rule 701, since state corporate law will generally require some documentation of the authorized issuance of equity securities. However, we urge the Commission to clarify that the requirement will be satisfied by resolutions adopted by the issuer's board of directors or other granting authority (*e.g.*, board committee or designated executive), as well as by less formal writings, such as memos or emails, since in our experience the equity granting process of start-up companies is often informal.

4. *The provision of financial statements to employees, former employees and other covered persons should not be a condition to reliance on the new Section 12(g)(5) safe harbor rule(s).*

We urge the Commission to adopt a safe harbor rule that does not include a requirement to deliver financial statements to employees and other covered holders of a class of equity securities as a condition to reliance on the Section 12(g)(5) carve-out for holders of compensatory plan securities. (Of course, an issuer relying on Rule 701 for the original issuance of the compensatory equity securities may have an independent obligation to deliver financial statements and other information if it sells more than $5 million worth of securities in any consecutive 12-month period, in accordance with Rule 701(e).) Section 503 of the JOBS Act does not mandate the delivery of financial statements as a condition to reliance on the Section 12(g)(5) carve-out for holders of compensatory plan securities, and does not even call upon the Commission to consider whether such a requirement is appropriate. While we acknowledge that a requirement to deliver financial statements is included in Exchange Act Rules 12h-1(f) and (g), we believe that these rules have not been widely used as a result of this requirement. Moreover, in our experience, companies go to great lengths to remain under the $5 million threshold in Rule 701 in order to avoid triggering the obligation to provide financial statements.

In sum, we believe that private companies are reluctant to provide financial statements to their employees out of a concern for the confidentiality of their financial results. If the applicable Securities Act exemption otherwise does not require provision of financial statements for the purchase of compensatory securities, we believe that such a requirement should not be imposed as a condition of the new safe harbor(s) implementing the compensatory plan carve-out of Section 12(g)(5).

5. *The safe harbor rule(s) should provide that, in the event of a subsequent transaction (including a business combination) that is exempt from, or otherwise is not subject to, the registration requirements of Section 5, the securities issued in that transaction to eligible employees, former employees, and other covered persons in exchange for securities covered by the Section 12(g)(5) compensatory plan securities carve-out (including any Commission safe harbor rule thereunder) also are covered by the Section 12(g)(5) carve-out.*

Non-reporting companies are frequently parties to restructurings, business combinations (involving either affiliates or non-affiliates) or other pre-IPO transactions in which their securities are exchanged for other securities in a transaction which is exempt from, or not subject to, the registration requirements of the Securities Act. The following are examples:

- A recapitalization in which a corporation issues its securities in exchange for other securities of the same corporation (*e.g.*, exchange of nonvoting stock for voting stock) in reliance on Section 3(a)(9) of the Securities Act.

- A statutory merger in which securities of one corporation are exchanged for securities of another, newly created corporation solely for the purpose of changing an issuer's domicile within the United States, in reliance on Rule 145(a)(2) under the Securities Act.

- The creation of a holding company through a reverse triangular merger in which securities of a newly-formed corporation are exchanged for securities of another corporation that becomes a wholly-owned subsidiary, in reliance on Section 3(a)(10) of the Securities Act.

In such transactions, if the securities being exchanged would have come within the Section 12(g)(5) carve-out from the application of the "held of record" definition, the securities issued in exchange also should come within that carve-out. In each of the three examples outlined above, the "business" of the issuer generally is substantially the same both before and after the exchange of securities, even though as a technical matter a different security or even a different "issuer" may be involved. In such cases, it would be an application of form over substance if the transaction caused loss of the Section 12(g)(5) carve-out.

We further recommend that the Commission consider extending favorable Section 12(g)(5) "carve-out" treatment to equity securities issued in exchange for compensatory plan equity securities within the broader framework of a business combination involving the acquisition by one non-reporting company of another non-reporting (and otherwise non-affiliated) company, in reliance upon a Securities Act exemption or exemptive safe harbors such as Securities Act Section 4(a)(2) and Regulation D thereunder, Section 3(a)(11) and Rule 147 thereunder, and Section 3(a)(10). While we acknowledge that this type of transaction involves the combination of two different issuers and may result in the creation of an entirely new and distinct surviving issuer, sound policy considerations support "passing through" the Section 12(g)(5) compensatory carve-out that attached to the compensatory equity securities of the target issuer to equity securities issued in the transaction to target holders of these carve-out eligible securities.[9] We believe that there are valid policy reasons for thus extending the Section 12(g)(5) carve-out to the new equity securities issued to target holders of compensatory plan securities that originally had the benefit of this carve-out. At a minimum, we urge the Commission to consider the valid policy reasons for recognizing such a "pass through" in situations where both the acquirer and target issuers are exempt from Section 12(g) registration at the time of the business combination, and the surviving and/or successor issuer remains below the Section 12(g) registration threshold (assuming that the equity securities issued in exchange for the acquired issuer's compensatory plan securities are subtracted from the Section 12(g) "holder of record" count undertaken by the surviving/successor issuer in reliance upon the Section 12(g)(5) carve-out).[10]

Any other result would compel a small non-reporting issuer to choose between participating in an acquisition which it believes is in the company's best interest, or accepting the need to "go public" via Exchange Act registration of the surviving/successor issuer's equity securities. Subjecting non-reporting issuers to such a choice not only would discourage the use of equity securities by small emerging growth issuers to compensate their employees, but also would penalize the type of pre-IPO "put-together" transaction that ultimately might better position a non-reporting issuer for a successful IPO. In either case, two important policy

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9 *Compare* Exchange Act Rule 12g-3(a) (in connection with a succession by merger, consolidation, an exchange of securities or similar transaction, the acquiring issuer securities not already registered under Section 12 of the Exchange Act will be deemed registered if issued to holders of target company securities that are so registered, unless the number of record holders of the newly issued class is less than 300). Although seemingly inapplicable to a succession by merger or otherwise involving two non-reporting companies, the policy rationale underpinning Rule 12g-3(a) – the protection of target record holders who enjoy the benefits of periodic reporting – is generally relevant here for the following reasons. Holders of compensatory equity securities of a non-reporting target company, who are not counted as recordholders for purposes of their employer's Exchange Act Section 12(g)(1) recordholder calculation because of amended Section 12(g)(5), should be able to receive equivalent compensatory equity securities from the acquiring company without risk to the latter company of exceeding the 2000-holder/ maximum 500 unaccredited holder threshold established by Title V of the JOBS Act (or Title VI in the case of banks). The ability of the non-reporting acquiring company to continue to use equity securities as compensation for employees "inherited" from the acquired company, without fear of being forced prematurely into an Exchange Act reporting regime, could preserve both the jobs of such employees post-acquisition and the flexibility of the acquiring company to grow via acquisition while remaining private.

10 In our view, the reasoning underlying the Division of Corporation Finance's Securities Act Rules Compliance and Disclosure Interpretation ("C&DI") 271.04, which had the effect of overturning the relief granted in the 1989 Devon Energy Corp. no-action letter (Devon Energy Corp. (May 12, 1989), enabling the non-reporting acquired company's compensatory options to be exercised for the public acquiror's stock under Rule 701 after consummation of the transaction and the public acquiror's assumption of the target's employee benefit plans), should not apply in the situation described in the above text. Under our example, two non-reporting issuers would be combining to create a non-public successor, which would assume the compensatory plan obligations of the target company.

underpinnings of the JOBS Act – *i.e.* to encourage small businesses to issue equity securities under compensatory plans without forcing premature registration of a class of such securities under Section 12(g), and to enable smaller non-reporting companies to delay entry into the public securities markets until they are prepared to bear the costs of becoming a registrant – clearly would be undermined.

Moreover, if the acquisition transaction just described were to trigger a loss of the Section 12(g)(5) carve-out, it would give rise to the anomalous situation in which employees of the acquired company (and their permitted transferees) in effect would be counted as record holders with respect to compensatory plan securities they received before the acquisition transaction, but existing employees of the acquiring issuer would continue to be excluded from the count with respect to compensatory plan securities issued after the transaction's consummation, even though both sets of equity securities would have been received under compensatory plans and presumably would be eligible for the Section 12(g)(5) carve-out. In our view, Congress could not have intended such an anomalous result in connection with pre-IPO combinations of small non-reporting companies.

6. *The safe harbor rule(s) should provide that the Section 12(g)(5) carve-out is not affected by the form in which the compensatory plan securities are held by employees, former employees or permitted transferees.*

Individuals often hold securities reflected in the books and records of the issuer in ways other than their individual names. For example, securities may be held jointly with a spouse (as community property, joint tenants, or tenants in common), as trustee (or co-trustee with spouse) of a revocable trust, or in a self-directed individual retirement account (IRA). All of these forms of ownership should be treated by the safe harbor rule as equivalent to ownership by the individual employee or permitted transferee for purposes of the Section 12(g)(5) carve-out.

Rule 12g5-1(a) provides that for purposes of determining whether an issuer is subject to Sections 12(g) and 15(d) of the Exchange Act, "securities shall be deemed to be 'held of record' by each person who is identified as the owner of such securities on records of security holders maintained by or on behalf of the issuer . . . ." Notwithstanding that general statement, the Rule then sets forth various situations in which securities are considered to be held of record by a single person, including the following:

- securities identified as held of record by one or more persons as trustees, executors, guardians, custodians or in other fiduciary capacities with respect to a single trust, estate or account;
- securities held by two or more persons as co-owners; and
- securities registered in substantially similar names where the issuer has reason to believe that such names represent the same person.

We believe that these provisions should be expressly made applicable to determinations of record holders for purposes of Section 12(g)(5), and that IRA and similar accounts should be added to the types of holdings treated as equivalent to holding by a single person.

7. *If a broad safe harbor rule (or rules) is adopted under Section 12(g)(5), Exchange Act Rule 12h-1(f) will no longer be necessary, but Rule 12h-1(g) may have continuing application.*

Rules 12h-1(f) and (g) provide exemptions from Exchange Act registration for compensatory stock options held by more than 500 holders of record if the conditions set forth in the rule are satisfied. Rule 12h-1(f) applies to issuers that are not subject to Exchange Act registration and/or reporting, and Rule 12h-1(g) applies to issuers that have a class of securities that is subject to Exchange Act registration and/or reporting.

We believe that Rule 12h-1(f) would no longer be necessary upon adoption of a safe harbor rule under Section 12(g)(5) having the scope described in this letter. In particular, the safe harbor would need to be broad enough to cover securities held by the persons identified in the definition of family member under Rule 701(c) who acquire the securities from the employee by gift, domestic relations order, or death, as well as executors and guardians of any such persons, and would need to cover securities issued under any exemption from registration under Section 5 of the Securities Act. Under such circumstances, we believe the new safe harbor rule would exempt all classes of securities currently exempted by Rule 12h-1(f).

However, with respect to an issuer that is subject to the Exchange Act reporting requirements, there may be instances in which securities of a class that is not registered under the Exchange Act are issued to employees for compensatory purposes under circumstances in which Securities Act registration is required, in which case the Section 12(g)(5) safe harbor rule would not be available. Since new compensation vehicles develop over time, we would suggest retaining Rule 12h-1(g) for such situations.

8. *The Commission should adopt a safe harbor rule that enables companies with a class of equity securities registered under Section 12(g) of the Exchange Act, or that are reporting under Section 15(d) of the Exchange Act, to return to private company status if they have fewer than 300 holders of record after applying the Section 12(g)(5) carve-out for holders of compensatory plan securities.*

Section 12(g)(4) of the Exchange Act provides for the termination of Exchange Act registration of a class of securities after the issuer files a certification with the Commission that the number of holders of record of such class is less than 300 persons. In addition, if the issuer has registered the class of securities under the Securities Act, it has an obligation under Section 15(d) of the Exchange Act to file Exchange Act reports, which obligation is suspended for any year (other than the year of Securities Act registration) in which the class is held by less than 300 persons. We urge the Commission to adopt a rule which would permit an issuer to determine whether a class has fewer than 300 holders of record under both of these provisions after excluding employees (and other covered persons, as discussed above) holding compensatory plan securities.

We believe that for a number of issuers, Exchange Act registration has been triggered prematurely by the issuance of compensatory plan securities to employees, and that the policies underlying the JOBS Act would support a rule under which such companies could return to private company status if so desired. Exchange Act Sections 12(g)(4) and 15(d) use the same concept of "holder of record" of a security as does Section 12(g)(1) of the Exchange Act – albeit with a lower numerical threshold – and it seems reasonable that holders excluded from the count under Section 12(g)(1) should also be excluded from the count under these sections. The Commission's current Rule 12g5-1 recognizes this by providing a definition of securities "held of record" that applies "[f]or purposes of determining whether an issuer is subject to the provisions of Sections 12(g) and 15(d) of the [Exchange] Act." However, in applying the Section 12(g)(5) carve-out to issuers that have already registered a class of securities under the Exchange Act, the carve-out for compensatory plan securities would need to be expanded to include securities issued pursuant to a registration statement on Securities Act Form S-8.[11]

9. *Issuers should be able to make determinations concerning the eligibility of employee compensatory plan equity securities for the Section 12(g)(5) carve-out during a reasonable period before or after the fiscal year-end, without having to make a separate judgment as of the end of the fiscal year in question.*

We urge the Commission to allow issuers the same flexibility in timing to determine the eligibility of equity securities for the compensatory plan securities carve-out as suggested above (in Part A.3.d. of this letter) for the "accredited investor" determination.

10. *The Section 12(g)(5) carve-out for employee compensatory plan equity securities, and any safe harbor or other Commission rule(s) implementing that carve-out, should apply to the determination by a bank or bank holding company of the number of record holders under Section 12(g)(1)(B), as amended by Title VI of the JOBS Act.*

We recommend that the Commission also clarify that the carve-out from the "held of record" definition for holders of employee compensatory plan securities set forth in Section 502 of the JOBS Act (amending Section 12(g)(5)), extends to banks and bank holding companies whose Section 12(g)(1)(B) record holder determination is governed by Section 601(a) of Title VI of the JOBS Act, and any Commission rulemaking thereunder pursuant to Section 602. Given the added flexibility accorded to these issuers in Title VI, with respect both to entering and exiting the Exchange Act reporting regime, we believe that such an extension would be entirely consistent with Congressional intent.

[11] In this regard, because Section 12(g)(5) by its terms is limited to equity securities issued pursuant to an employee compensation plan in reliance upon a Securities Act exemption, we recognize that the Commission might find it necessary to invoke its general exemptive authority under Exchange Act Section 36(a) to achieve the result recommended in the text.

C. The Crowdfunding Securities Exemption Under Exchange Act Section 12(g)(6)

Section 12(g)(6) of the Exchange Act, which was added by Section 303(a) of the JOBS Act, requires the Commission to adopt a rule "to exempt, conditionally or unconditionally, securities acquired pursuant to an offering made under section 4(6) of the Securities Act of 1933" from the registration requirements of Section 12(g) of the Exchange Act. The suggestions set forth below are intended to assist the Commission in promulgating proposed rules under this section.

1. *The Commission should confirm that the exemption applies to, and flows with, the securities initially acquired in a crowdfunding offering, and that the exemption therefore is not limited to securities in the hands of initial purchasers in that offering.*

Section 12(g)(6) provides that the rule should exempt from registration under Section 12(g), either "conditionally or unconditionally, securities acquired pursuant to an offering made under Section 4(6) of the Securities Act of 1933…." We believe that this language is best read to mean that the Section 12(g) exemption attaches to the securities issued in a crowdfunding offering made under Section 4(6) – meaning that the exemption travels with the securities after their transfer by the initial purchaser (whether for consideration or via gift, etc.) to subsequent holders, and therefore should not be limited to securities in the hands of the initial purchasers in such an offering.[12]

In our view, the most logical and appropriate interpretation of new Exchange Act Section 12(g)(6), one that is entirely consistent with the capital formation purposes of Securities Act Section 4(6) and the inclusion of this new Section 12(g) exemption in Title III rather than Title V, is to apply the Section 12(g) exemption to the <u>securities</u> issued in a Section 4(6)-exempt crowdfunding offering, such that the Section 12(g) exemption continues to be available once the securities are sold or otherwise transferred by the initial purchaser of such securities. Unlike the Title V amendments excluding holders who are accredited investors or "securities held by persons who received" the securities pursuant to an employee compensation plan, new Section 12(g)(6) references only the securities and not the current holder. We think the most analogous provision is the definition of "restricted security" set forth in Securities Act Rule 144(a)(3), which encompasses "securities acquired" in a variety of exempt transactions and imposes resale restrictions on subsequent holders, not just the person who acquired the securities in the exempt transaction.

We believe a Section 12(g) exemption limited to the initial purchaser of crowdfunding

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[12] A review of the legislative history indicates that the original text of the bill introduced in the House of Representatives would have excluded from the Section 12(g) count those equity securities "issued" in a crowdfunding transaction. However, the language was revised by amendment to change it to securities held by "persons who purchase" in such transactions. The final language of the statutory provision, which refers to "securities acquired" in a crowdfunding transaction, originated in the Senate and changed only in respect of mandating, rather than just authorizing, Commission rulemaking *See* Cong. Rec. S1886-S1888, S1894-S1895 (March 21, 2012).

securities would undermine the utility of such an exemption, because the issuer would be forever exposed to a "springing" Section 12(g) reporting obligation in the event the initial purchaser were to sell his or her equity securities, which in many instances could occur without the issuer's knowledge. An initial purchaser should not be able to force an issuer to register under Section 12(g) simply by reselling his or her securities. Therefore, we strongly recommend that the Section 12(g)(6) exemption apply to the securities issued in a crowdfunding offering, and consequently, remain valid upon the resale or transfer of such securities by the initial purchaser.

To be clear, we do not believe that the Section 12(g)(6) exemption should be available to holders that also own equity securities of the issuer that were not issued pursuant to an offering made under Section 4(6). In this regard, a holder of both crowdfunding securities and non-crowdfunding securities should be counted for purposes of Section 12(g)(1), unless the non-crowdfunding securities are eligible for a separate exemption under Section 12(g). For example, if a holder owns 100 shares of ABC Corp. common stock acquired in a crowdfunding offering under Section 4(6) (the " C Shares") and 100 shares of ABC Corp. common stock acquired in a Rule 506 offering under Regulation D of the Securities Act (the "D Shares"), such holder should be counted for purposes of Section 12(g)(1), absent a separate exemption in respect of the D Shares. However, if the holder sold all of his or her D Shares and retained only the C Shares, the issuer should be entitled to omit the holder for Section 12(g)(1) counting purposes because all securities held by such person would be exempt under Section 12(g)(6).

2. The rule should provide that the exemption survives and attaches to different securities issued in a subsequent restructuring, recapitalization or similar transaction that is exempt from, or otherwise not subject to, the registration requirements of Section 5, so long as the parties to the subsequent transaction are affiliates of the original issuer.

Non-reporting companies are frequently parties to restructurings, recapitalizations and other transactions in which their securities are exchanged for other securities in a transaction that is exempt from, or otherwise not subject to, the registration requirements of the Securities Act. Examples of these transactions include (but are not necessarily limited to): (i) a recapitalization under Section 3(a)(9) of the Securities Act; (ii) a statutory merger to change the domicile of the issuer, in reliance on Rule 145(a)(2) under the Securities Act; and (iii) creating a holding company through a reverse triangular merger, in reliance on Section 3(a)(10) of the Securities Act.[13]

In such transactions, if the securities being exchanged come within the Section 12(g)(6) exemption by virtue of having been acquired in a crowdfunding offering made under section 4(6) of the Securities Act, the securities issued in exchange for those securities by the original issuer or by an affiliate of that issuer also should come within the Section 12(g)(6) exemption. We think this is appropriate here because, in the above examples, the "business" of the issuer is the same both before and after the exchange of securities, even though as a technical matter a different security or different (albeit affiliated) "issuer" may be involved. In such cases, we

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[13] For additional description of these types of pre-IPO transactions, see Part B.5. of this letter

believe that it would be an application of form over substance if the transaction caused loss of the Section 12(g)(6) exemption.

As discussed above, the Exchange Act Section 12(g)(6) exemption attaches to the securities issued in a crowdfunding transaction covered by Securities Act Section 4(6), without regard to who holds them – in contrast to the "holder-focused" approach taken by Congress with respect to equity securities of non-reporting issuers held by employees who received them for compensatory purposes under Section 12(g)(5), or held by "accredited investors" under Section 12(g)(1)(A). Because of this significant difference in the relevant statutory language, we do not believe it would be appropriate for the Commission to extend Section 12(g)(1) exemptive treatment by rule to equity securities issued by an unaffiliated third party in a business combination or similar transaction in exchange for the target company's "crowdfunded" equity securities (unless, of course, the acquiring company is otherwise permitted by Commission rulemaking under Title III to rely on the Securities Act Section 4(6) exemption to issue a new class of "crowdfunded" securities as consideration for the acquisition transaction). In particular, the policy rationale for allowing a "pass-through" of the Exchange Act Section 12(g)(5) carve-out for target employees (and other persons covered by Securities Act Rule 701) in a business combination context is absent in the case of securities acquired in an exempt crowdfunding transaction.

3. *The availability of the exemption set forth in Exchange Act Section 12(g)(6), and/or any safe harbor the Commission adopts thereunder, should be conditioned on: (a) issuance of the securities in question in a transaction that qualifies for the Securities Act Section 4(6) exemption; or (b) the issuer's reasonable belief, at the time of the annual Section 12(g) determination, that the Section 4(6) exemption (and/or an exemptive safe harbor thereunder) was available in connection with the original crowdfunding transaction. But only post-transaction obligations that are within the issuer's control should be considered in determining whether the exemption's conditions were met.*

In our view, the Commission should implement Section 12(g)(6) by requiring that either: (a) the predicate crowdfunding transaction in fact qualified for the Securities Act Section 4(6) exemption, which conditions the availability of the exemption upon satisfying certain requirements applicable to intermediaries (Section 4A(a)) and issuers (Section 4A(b)); or (b) the issuer have a reasonable belief, at the time of making its annual Section 12(g) record holder determination, that the securities in question were acquired in a transaction exempt under Section 4(6) of the Securities Act.

With respect to an issuer's post-offering performance of its annual filing and disclosure obligations (as prescribed in Securities Act Section 4A(b)(4)), as a condition to reliance on the Securities Act Section 4(6) exemption – which in turn will affect that issuer's ability to exclude from the annual Section 12(g) record holder count those securities "acquired" in the original crowdfunding offering pursuant to the exemption set forth in Exchange Act Section 12(g)(6) – we recommend that the Commission focus solely on those obligations that are within the exclusive control of the issuer. In this connection, Section 4A(b)(4) requires an issuer that offers or sells securities under Securities Act Section 4(6) to file with the Commission on at least an annual basis, and to provide to investors, such reports of the results of operations and financial statements of the issuer as the Commission, by rule, determines appropriate. While we acknowledge that the practical impact of disallowing reliance on the Exchange Act Section 12(g)(6) exemption by a delinquent issuer may be to impose even more rigorous reporting (and registration) obligations under Section 12(g), we believe this result is warranted as a meaningful enforcement mechanism.

We do not, however, recommend conditioning the availability to the issuer of the Section 12(g)(6) exemption on non-affiliated third parties' compliance with post-crowdfunding offering obligations that arguably are outside the control of the issuer.[14] The risk of a *post hoc* invalidation of the Securities Act Section 4(6) exemption – and thus the Exchange Act Section 12(g)(6) exemption – on the basis of actions outside the control of the issuer would substantially increase the risk that an issuer would later become subject to Exchange Act registration and reporting obligations (and possibly also a Securities Act Section 5 violation), and thereby greatly increase the potential costs of using crowdfunding as a vehicle for equity financing. Such a result would seem to undermine Congress's intent that crowdfunding stimulate small business capital-raising without exposing non-reporting issuers to the full panoply of Exchange Act registration and reporting requirements.

We suggest that the Commission provide illustrative (but non-exclusive) guidance as to the appropriate foundation for an issuer's "reasonable belief" that the securities in question were issued in a Section 4(6)-exempt crowdfunding transaction. Such guidance could appear in the regulatory text or in the accompanying release, and might include a non-exclusive list of factors the issuer may consider in determining whether specified equity securities originally were issued in a Section 4(6) transaction, such as (i) use by the issuer of a separately designated class of securities in crowdfunding offerings (*e.g.,* only "Class C" securities are issued), (ii) application of a stock legend, and/or (iii) use of a share numbering system specific to the crowdfunding securities (*e.g.*, shares numbered 1 to 100 are crowdfunding securities). That said, we do not recommend that the Commission impose a formal "tracing" obligation or otherwise prescribe the specific method(s) by which identification of equity securities, at the time the annual Section 12(g) record holder count is taken, as having been "acquired pursuant to an offering made under section 4(6) of the Securities Act" should be undertaken. Instead, the Commission should permit a flexible approach that would enable the issuer and other market participants to develop – as has been the case under Securities Act Rule 144 – whatever approach the parties deem most efficient and effective in meeting the conditions of Exchange Act Section 12(g)(6) and/or any rules the Commission must adopt thereunder.

[14] It is impossible to predict at this point whether any entity other than the issuer in fact will have substantive post-transactional obligations that, if not performed, could operate retroactively to destroy an otherwise valid Securities Act Section 4(6) exemption (and thus, the Exchange Act Section 12(b)(6) exemption). However, we note that the Commission has been given broad authority potentially to impose such obligations on intermediaries (Securities Act Section 4A(a)(12)) as well as the issuer itself (Section 4A(b)(5)). In addition, the issuer as a practical matter will not necessarily be able to police resales by non-affiliated investors.

4. *The availability of the exemption under Section 12(g)(6), and/or any exemptive safe harbor or other rules adopted thereunder, should be conditioned on the issuer not having total assets, at the last day of the fiscal year with respect to which the Section 12(g) compliance determination is made (or a reasonable time before or after such date), in excess of $25 million.*

We recommend that the Commission's proposed rule provide that the Section 12(g)(6) exemption not apply to any issuer that had assets, at the last date of the fiscal year with respect to which the Section 12(g) compliance determination is made, in excess of $25 million. Imposing such a requirement would avoid the inconsistency that certain companies with lesser amounts of assets, but which had grown by means other than crowdfunding, would be required to become publicly reporting companies, while companies that had grown to a much larger size, with hundreds or perhaps thousands of shareholders, would be exempt from Section 12(g) registration.

5. *The Commission should extend any Section 12(g)(6) exemptive safe harbor rules to eligible banks and bank holding companies that engage in exempt crowdfunding offerings under Section 4(6) of the Securities Act.*

For the reasons discussed above in Part B.10. of this letter, we recommend that the Commission extend the availability of the Exchange Act Section 12(g)(6) exemption to banks and bank holding companies whose Section 12(g)(1)(B) record holder determination is governed by Title VI of the JOBS Act.

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The Committee appreciates the opportunity to submit these comments. Members of the Committee are available to meet and discuss these matters with the Commission and its staff and to respond to any questions.

Very truly yours,

/s/ Catherine T. Dixon
Catherine T. Dixon
Chair, Federal Regulation of Securities Committee

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