

BRIEFING

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Corporate & Securities
Practice Group

SEC Proposes Modernization of Smaller Company Capital-Raising and Disclosure Requirements

On May 23, 2007, the SEC proposed several modifications to its existing regulation of small business issuers. "Small business issuers" are U.S. or Canadian public companies with less than \$25 million in revenues and a public float of \$25 million or less. Currently, small business issuers are permitted to use shorter disclosure forms (i.e., "SB" forms) that require less disclosure than standard SEC forms. These proposals would also make helpful changes to Regulation D (the private offering safe harbor) and Rules 144 and 145 (the resale safe harbors).

Smaller Reporting Company Simplification

The SEC proposed making the lessened disclosure and reporting requirements applicable to smaller companies available to most companies with up to \$75 million of public float.

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To simplify the regulatory framework, the SEC proposed combining the "small business issuer" and "non-accelerated filer" categories of smaller companies into a new category of "smaller reporting companies." In connection with this proposal, disclosure requirements under Regulation S-B would be

integrated into Regulation S-K and the related "SB" forms would be discontinued.

The SEC also proposed making Form S-3 and Form F-3 (including "shelf" registration) available to companies with less than \$75 million of public float, provided that they: (1) do not sell more than 20% of their public float

in primary offerings on those forms in any one-year period, (2) have timely filed all SEC reports for the past year, and (3) are not at the time of filing, and have not been at any time in the last year before filing, "shell companies."

Exemption of Compensatory Stock Options from Registration

Under a proposed amendment to Section 12(g) of the Securities

Exchange Act, private, non-reporting companies would be exempt from registering compensatory employee stock options issued under a written compensatory stock option plan, provided that: (1) eligible options holders are limited to employees, directors, consultants, and advisors, (2) transferability of the shares received on exercise of such option are restricted, and (3) risk and financial information is disclosed to option holders and holders of shares received on exercise of options. Currently, a private company with 500 or more shareholders or option holders and more than \$10 million in assets would be required to register and file reports with the SEC under the Securities Exchange Act. This exemption would not extend to the class of securities underlying the options, however. The SEC also proposed a separate exemption

**ISSUERS SELLING TO A NEW
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CALLED "RULE 507 QUALIFIED
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for issuers that have registered common stock underlying the compensatory stock options.

Regulation D Limited Offering Exemption

The SEC proposed establishing a new exemption from the Securities Act's registration provisions under Rule 507 of Regulation D. Issuers selling to a new category of investors called "Rule 507 qualified purchasers" could sell securities through limited advertising without registration. Rule 507 qualified purchasers would include: (1) certain institutional investors, (2) individuals who own \$2.5 million in investments or have an annual individual income of \$400,000 or aggregate income of \$600,000 with their spouses, and (3) directors, executive officers, and general partners of the issuer, without regard to a monetary threshold.

The proposed amendments would also increase the number of investors qualified as "accredited investors" by revising the existing definition to include individuals with \$750,000 and institutions with \$5 million of owned investments. The thresholds for accredited investors would be adjusted for inflation in the future, beginning in 2012.

The SEC proposed to decrease Regulation D's integration safe harbor from six months to 90 days and to update "bad actor" disqualifications such that they apply to all offerings under Regulation D (not just offerings under Rule 505 per current Regulation D).

Mandatory Electronic Filing of Form D

The SEC proposed that companies be required to file Form D electronically. Form D is required to be filed by companies that have sold securities without registration relying on an exemption under Regulation D. As Form D must currently be filed on paper, a new online filing system would be created to enable companies to file from any computer with internet access. Information would be searchable by regulators and members of the general public. The SEC also proposed that Form D itself be simplified and restructured.

Amendments to Securities Act Rules 144 and 145

The SEC proposed amendments to Rule 144 of the Securities Act to shorten the holding period to six months, eliminate restrictions on resale of securities by non-affiliates after a one-year period (currently it is two years), and raise the thresholds triggering a Form 144 filing. The SEC also proposed to revise Rule 145 of the Securities Act to eliminate restrictions on resale of securities received in Rule 145 transactions (e.g., business combinations), except with regard to transactions involving shell companies.

The proposing release containing additional details on these initiatives will be published by the SEC shortly.

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