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Securities Alert

SEC Proposes Exchange Act Rule Amendments

Last week, the SEC proposed amendments to various rules adopted primarily under Section 12(g) of the Securities Exchange Act of 1934 (the "Exchange Act") to reflect the new, higher thresholds for registration, termination of registration and suspension of reporting established by Title V and VI of the Jumpstart Our Business Startups Act (the "JOBS Act"); to specify the definitions of "accredited investor" and "record holders" to be used in making such determinations; and to expand the application of the new thresholds to savings and loan holding companies.

Reporting Thresholds

Prior to the enactment of the JOBS Act, Section 12(g) of the Exchange Act required an issuer to register a class of its equity securities if, at the end of the issuer's fiscal year, the securities were "held of record" (see below for proposed amendments to this definition in accordance with the JOBS Act) by 500 or more persons and the issuer had total assets exceeding $1 million. An issuer that had a class of equity securities registered under Section 12(g) was able to terminate that registration if the number of record holders of that class fell below 300, or the number of record holders of that class fell below 500 and the issuer's assets were no more than $10 million at the end of each of its last three fiscal years. In addition, an issuer's reporting obligation under Section 15(d) of the Exchange Act was automatically suspended under Section 15(d)(1) if, on the first day of any fiscal year other than the year in which the registration statement became effective, there were fewer than 300 holders of record of the class of securities offered under the registration statement.

The JOBS Act amended Sections 12(g) and 15(d) of the Exchange Act to adjust these thresholds for registration, termination of registration and suspension of reporting.

Section 501 of the JOBS Act amended Exchange Act Section 12(g)(1) to require an issuer (other than a bank or a bank holding company, as defined in Section 2 of the Bank Holding Company Act of 1956) 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 the class of equity securities is "held of record" by either: (i) 2,000 persons; or (ii) 500 persons who are not "accredited investors." Section 601 of the JOBS Act amended Exchange Act Section 12(g)(1) to require a bank or a bank holding company issuer to register a class of equity securities (other than exempted securities) within 120 days after the last day of its first fiscal year ended after the effective date of the JOBS Act 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.

Section 601 of the JOBS Act also amended Exchange Act Section 12(g)(4) and Exchange Act Section 15(d)(1) to enable an issuer that is a bank or a bank 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 in Section 12(g)(4) for termination of registration and in Section 15(d)(1) for suspension of reporting remains at 300.

Although the amendments to the Exchange Act sections described above became effective on the effective date of the JOBs Act, the corresponding Exchange Act rules still reflect the prior statutory thresholds. As a result, the proposals would amend Rule 12g-1 to reflect the asset and holder of record thresholds established by the JOBS Act relating to the requirement to register a class of equity securities under the Exchange Act, and amend Rules 12g-2 and 12g-3 to reflect the new holders of record thresholds for terminating registration and suspending reporting for banks and bank holding companies.

In addition, although Exchange Act Section 12(g) and 15(d) do not suspend reporting obligations immediately when an issuer reaches the designated threshold, Rules 12g-4 and 12h-3 permit issuers to immediately suspend their duty to file periodic and current reports. These rules, however, reflect the thresholds in Sections 12(g) and 15(d) prior to the JOBS Act amendments and not the new threshold for banks and bank holding companies. Because the new statutory threshold for banks and bank holding companies is not reflected in Rule 12g-4, banks and bank holding companies seeking to rely on the new 1,200-holder threshold may not rely on the existing procedural accommodations in the rule. As a result, the statute requires them to wait 90 days after filing a certification with the SEC that the number of holders of record is less than 1,200 persons to terminate their Section 12(g) registration and cease filing reports required by Section 13(a) rather than being able to suspend their Section 13(a) reporting obligations immediately upon the filing of a Form 15 in reliance on the rule. Similarly, banks and bank holding companies are not permitted to rely on Rule 12h-3 to immediately suspend their Section 15(d) reporting obligations using the new higher statutory threshold during a fiscal year. Rather, Section 15(d)(1) provides that they may use the higher thresholds only when seeking to suspend a Section 15(d) obligation on the first day of a fiscal year.

The proposed changes would allow banks and bank 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.

Savings and Loan Holding Companies

The proposals would also apply the same thresholds to savings and loan holding companies (which are not covered by Title VI of the JOBS Act) that apply to banks and bank holding companies, by establishing an exemption from registration requirements under Rule 12g-1 for such entities that mirrors the exemption for banks and bank holding companies established by the JOBS Act. In addition, the proposal would revise Rules 12g-2, 12g-3, 12g-4 and 12h-3 to permit savings and loan holding companies to immediately suspend current and periodic reporting upon filing Form 15 at the 1,200-holder threshold in the same manner as banks and bank holding companies.

Accredited Investors

To rely on the new, higher threshold established by the JOBS Act, an issuer will need to be able to determine which of its record holders are accredited investors. The proposal specifies that the definition of "accredited investor" in Securities Act Rule 501(a) would apply in making determinations under Exchange Act Section 12(g)(1), and that the accredited investor determination would be made as of the last day of the most recent fiscal year.

Record Holders

Section 502 of the JOBS Act amended Exchange Act Section 12(g)(5) to exclude from the definition of "held of record" (for the 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 of 1933 (Securities Act). Section 503 of the JOBS Act instructed the SEC to implement this exclusion, and to create a safe harbor for issuers when determining whether holders received their securities pursuant to an "employee compensation plan" in a transaction exempted from the registration requirements of Section 5 of the Securities Act. This statutory exclusion applies solely for purposes of determining whether an issuer is required to register a class of equity securities under the Exchange Act (not to a determination of whether such registration may be terminated or suspended), and the term "employee compensation plan" is not defined.

The proposal would amend the definition of "held of record" to provide that when determining whether an issuer is required to register a class of equity securities 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; or

- held by persons eligible to receive securities from the issuer pursuant to Securities 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 the proposed definition.

Although the proposal does not define "employee compensation plan," it includes a non-exclusive safe harbor that would provide that a person will be deemed to have received the securities pursuant to an employee compensation plan if such person received them pursuant to a compensatory benefit plan in transactions that met the conditions of Securities Act Rule 701(c). Thus, instead of defining the term "employee compensation plan," the safe harbor relies on the current definition of "compensatory benefit plan" in Rule 701 and the conditions in Rule 701(c). Because the safe harbor would be limited to holders who are persons specified in Rule 701(c) who received the securities under specified circumstances, once these persons subsequently transfer the securities, whether or not for value, the securities would need to be counted as held of record by the transferee for purposes of determining whether the issuer is subject to the registration and reporting requirements of Exchange Act Section 12(g)(1).

In addition, foreign private issuers would be able to rely on the safe harbor under the proposed rules when making their determination of the number of US resident holders under Exchange Act Rule 12g3-2(a).

The SEC has made an extensive request for comments on the proposal, which must be received within 60 days of its publication in the *Federal Register*.

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