LET SLEEPING REGS LIE: A DIATRIBE ON REGULATION A'S FUTILITY BEFORE AND AFTER THE J.O.B.S. ACT

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Did Congress do the right thing when it attempted to revise Regulation A through Title IV of the J.O.B.S. Act or was their legislative effort an exercise in futility?

On April 4 2012, President Obama signed into law the J.O.B.S. (Jumpstart Our Business Startups) Act. The Act's intent is to ease the regulatory burden on smaller companies when issuing securities in both private and public offerings. This paper's specific focus is on the Act's Title IV. Title IV makes revisions to Regulation A, a private securities offering exemption promulgated under the Securities Act of 1933.

A big problem with Regulation A historically is that the provisions were burdensome, costly, and time consuming. In addition to a Federal component that required the issuer to file an offering statement with the Securities and Exchange Commission, Regulation A also requires that the issuer meet filing requirements within each state jurisdiction in which the issuer planned on offering its securities.[1] The heavy compliance burden was coupled with the fact that the most you could raise through a Regulation A offering was $5 million.[2] As a result, Regulation A has historically been all but dormant in use.[3]

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1. *See generally* 15 U.S.C. § 77r (2012) (exempting under Section 18 of the Securities Act of 1933 certain securities and securities offerings from state registration, but not exempting offerings made under Regulation A (pre-J.O.B.S. Act)).

2. 17 C.F.R. § 230.251(b) (2014) (pre-J.O.B.S. Act) *amended by* 17 C.F.R. pt. 230 (2015).

3. *See* U.S. GOV'T ACCOUNTABILITY OFFICE, GAO-12-839, SECURITIES REGULATION: FACTORS THAT MAY AFFECT TRENDS IN REGULATION A OFFERINGS (2012), at 9, Figure 1. The Report conveys Regulation A's declining use which peaked at 116 filings in 1997 and has declined steadily through 2011 where there were only 19 Regulation A filings in 2011.

The J.O.B.S. Act's Title IV has sought to remedy this by making several changes to Regulation A; the most noteworthy of which involves raising the offering ceiling from $5 million to $50 million. The question then is will this be enough to offset the compliance burdens that historically have kept issuers from using Regulation A. This paper takes a critical look at the changes to Regulation A mandated under the J.O.B.S. Act and concludes that Congress missed the mark yet again with its Regulation A revisions.

Congress should have left Regulation A alone as a poorly conceived regulation that was flawed at its initial inception. Not quite an exposé, this paper calls to task Congress' legislative thought process in the area of securities offering exemptions and seeks to hold them accountable for creating a revised offering exemption without regard for its potential end users.

INTRODUCTION

Though the law is a learned profession steeped in the art of problem solving, in some instances, the solution is simply to leave it alone as hard as that may be for us to accept. And that's okay. Accepting this reality frees us to deal with other endeavors more worthy of our time.

On April 8, 2014, Luis A. Aguilar, one of the five appointed Securities and Exchange Commission (SEC) Commissioners, stood before an audience of anxious state securities regulators and used all the tact and diplomacy that he could bring to bear to ease their concerns regarding the Commission's proposed rulemaking changes to the private securities exemption known as Regulation A. The proposed rules then being considered would greatly reduce the state regulator's role in overseeing Regulation A offerings in their respective jurisdictions.[4]

In a similar reaction to the Commission's proposed rulemaking, on June 3, 2014, a group of 20 House Democrats signed a letter written to SEC Chairman Mary Jo White stating that the SEC's proposed "Regulation A Plus" rules preempt state law too broadly, contrary to Congress' intent.[5] Finally, the North American Securities Administrators Association (NASAA) sent a strongly worded letter to the Commission, attacking the

4. Luis A. Aguilar, SEC Comm'r, Comments at the North American Securities Administrators Association Annual NASAA/SEC 19(d) Conference in Washington D.C. (Apr. 8, 2014), http://www.sec.gov/News/Speech/Detail/Speech/1370541436767#.VMpWgxfnbcs, *archived at* http://perma.cc/52BB-69XW.

5. Letter from Stephen F. Lynch et al., Members of Cong., to Honorable Mary Jo White, Chair, SEC (June 3, 2014), https://www.sec.gov/comments/s7-11-13/s71113-114.pdf, *archived at* https://perma.cc/P9AD-C2MZ.

proposed changes to Regulation A on many fronts and questioning the proposed rules' legality.[6] What started as a bid to make Regulation A a more user friendly[7] private placement exemption for issuers has mushroomed into a quagmire that has done nothing but reveal the flaws that existed before Regulation A was modified and that still remain after its revisions.

At times lawmakers get off track because they fail to ask the right question. During senate hearings on Regulation A and other capital formation issues, Senator Shelby asked, "[A]re there any changes that could be made to make Regulation A more appealing . . . ?"[8] But the more pointed question should have been, "Does Regulation A fill any unmet need or purpose in the realm of private securities offerings?" If Congress would have explored the situation by asking the appropriate threshold question, their whole approach to Regulation A may have taken a completely different path. Instead, Congress has engaged in a futile effort to revive Regulation A with legislative action through Title IV of the Jumpstart Our Business Startups (J.O.B.S.) Act.[9]

Congress' effort to revive Regulation A was an ill-conceived endeavor that never should have occurred. Congress should have accepted the fact that Regulation A is a private placement option that has moved to near extinction for two reasons: 1) Regulation A at its inception was too cumbersome, too time-consuming, and too costly to be a viable option for most issuers, where the maximum amount of money an issuer could raise in

6. *See* Comment Letter from Andrea Seidt, President, N. Am. Sec. Adm'rs Ass'n, Inc., to Elizabeth M. Murphy, Sec'y, SEC (Mar. 24, 2014), http://www.sec.gov/comments/s7-11-13/s71113-75.pdf, *archived at* http://perma.cc/G3V4-NP9J. (questioning the Commission's authority to define key terms, arguing for state-run alternatives to the proposed regime, and providing additional cost-benefit analysis to highlight problems with the proposed regime).

7. *Spurring Job Growth Through Capital Formation While Protecting Investors—Part I: Hearing Before the Comm. on Banking, Hous., & Urban Affairs*, 112th Cong. 25-26 (2011) (inquiry from Sen. Richard Shelby, Ranking Member, Comm. on Banking, Hous., & Urban Affairs), http://www.gpo.gov/fdsys/pkg/CHRG-112shrg74738/html/CHRG-112shrg74738.htm, *archived at* http://perma.cc/2G6S-JMU6.

8. *Spurring Job Growth Through Capital Formation While Protecting Investors—Part I: Hearing Before the Comm. on Banking, Hous., & Urban Affairs*, 112th Cong. 25-26 (2011) (inquiry from Sen. Richard Shelby, Ranking Member, Comm. on Banking, Hous., & Urban Affairs), http://www.gpo.gov/fdsys/pkg/CHRG-112shrg74738/html/CHRG-112shrg74738.htm, *archived at* http://perma.cc/2G6S-JMU6.

9. *See generally* Jumpstart Our Business Startups Act (J.O.B.S. Act), Pub. L. No. 112-106, 126 Stat. 306 (2012) (codified as amended in scattered sections of 15 U.S.C.), http://www.gpo.gov/fdsys/pkg/BILLS-112hr3606enr/pdf/BILLS-112hr3606enr.pdf?n=07083, *archived at* http://perma.cc/D7D2-VG8W; *see also* Jumpstart Our Business Startups Act tit. IV ("Small Company Capital Formation").

any twelve month period was $5 million;[10] and 2) a closer look at the few issuers who decided to go the Regulation A route reveal that their filings could have been achieved under a less costly, less cumbersome exemption if they had given the threshold decision of which exemption might be best a bit more thought.[11] This paper delves into this matter to reveal the conclusion that Congress should have come to on its own had they asked the right questions. No attempt should have been made to revive Regulation A's use. Regulation A was a flawed and ill-conceived exemption at its inception and should have been left to extinction. This paper will lay out the reasons for this conclusion.

The paper is organized as follows: Section I provides foundational knowledge regarding the J.O.B.S. Act in general and Title IV, the provision that revises Regulation A, in particular. Section II discusses the cumbersome aspects of Regulation A to bolster the reasons for Regulation A's historical lack of use. Section III supplies actual data showing Regulation A's use, or lack thereof, compared to other private offering exemptions that are less expensive, less time-consuming, and less cumbersome for the issuer. Section IV then explains the modifications the J.O.B.S. Act has made to Regulation A, the most notable of which is raising Regulation A's offering cap from $5 million to $50 million. There are other revisions as well, some of which have been and remain the basis of controversy and debate as of this article's publication date. The revisions and controversies surrounding some of the proposed changes will be discussed in Section IV as well. Section V posits the question of whether the modifications to Regulation A as promulgated under the J.O.B.S. Act will manifest itself in the form of issuers selecting Regulation A with more frequency compared to historical numbers. Section V takes the position that Regulation A as modified will not result in issuers selecting Regulation A with any greater frequency and explains the reasons for this conclusion. Section VI explains one of the more controversial aspects of Regulation A: namely the SEC's final rules which preempt Regulation A filings from all state registration and filing requirements for offerings exceeding $20 million. The intent is to explain the controversy surrounding this significant change to Regulation A and tie it into the overall argument as to why Regulation A's cumbersome aspects far outweigh any benefits that might be derived from using the exemption. Section VII suggests changes that could be made to Regulation A that

10. Securities Act of 1933, 17 C.F.R. § 230.251(b) (2014) (amended by 17 C.F.R. § 230.251(b) (2015)).

11. *See* discussion *infra* Part IV (arguing that exemptions issued under Regulation A are rare and have been improperly assigned).

might give it a better chance at being a viable offering exemption. Finally, Section VIII concludes.

I. THE J.O.B.S. ACT AND REGULATION A

A. *The J.O.B.S. Act in General*

On April 5, 2012, President Obama signed into law the Jumpstart Our Business Startups (J.O.B.S.) Act.[12] The Act's intended purpose is to ease the regulatory burden on small businesses when going public and operating as publicly held companies.[13] The Act consists of seven titles.[14] This article focuses on the Act's Title IV – *Small Company Capital Formation*. Title IV undertakes the noble but questionable endeavor of revising a flawed and seldom-used securities offering exemption with the hope of making the exemption a more viable and appealing option for issuers seeking a private placement exemption.[15] The exemption in question is referred to as Regulation A.[16] Prior to the proposed revisions under the J.O.B.S. Act, Regulation A allowed those filing under its exemption to offer up to $5 million worth of equity shares without having to register them.[17]

But Regulation A historically has not been used very much and over

12. Mark Landler, *Obama Signs Bill to Promote Start-Up Investments*, N.Y. TIMES, Apr. 5, 2012, at A12, http://www.nytimes.com/2012/04/06/us/politics/obama-signs-bill-to-ease-investing-in-start-ups.html?_r=0&pagewanted=print, *archived at* https://perma.cc/W5AT-P6V2.

13. *See Spurring Job Growth Through Capital Formation While Protecting Investors—Part I: Hearing Before the Comm. on Banking, Hous., & Urban Affairs*, 112th Cong. 1 (2011) (opening statement of Sen. Tim Johnson, Chairman, Comm. on Banking, Hous., & Urban Affairs), http://www.gpo.gov/fdsys/pkg/CHRG-112shrg74738/html/CHRG-112shrg74738.htm, *archived at* http://perma.cc/2G6S-JMU6 ("We are here to discuss how to help startups and businesses get access to the capital they need to grow and to create new jobs, while protecting investors.").

14. *See* J.O.B.S. Act, Pub. L. No. 112-106, 126 Stat. 306, § 2 (2012), http://www.gpo.gov/fdsys/pkg/BILLS-112hr3606enr/pdf/BILLS-112hr3606enr.pdf?n=07083, *archived at* http://perma.cc/D7D2-VG8W (listing the seven titles in the table of contents).

15. *See* Shelby *supra* n. 8 at 25-26. (during the hearing, Senator Shelby noted when speaking to Meredith Cross, Director, Division of Corporate Finance, Securities and Exchange Commission, "As you noted in your testimony, last year [2010] only three Regulation A filings were qualified by the SEC. So far this year not a single Regulation A filing has been cleared").

16. Regulation A, 17 C.F.R. § 230.251–.263 (2015).

17. 17 C.F.R. § 230.251(b) (pre-J.O.B.S. Act) (amended by 17 C.F.R. § 230.251(b)) (2015).

time has become close to dormant as companies have sought other less cumbersome exemptions that allow them to raise more money in less time and at a fraction of the cost.[18] In response to Regulation A's historical lack of use, Congress has made revisions to Regulation A through the J.O.B.S. Act's Title IV with the intent of making Regulation A a more appealing and viable option. Under these revisions, Regulation A is now referred to as Regulation A+.[19]

This paper critiques this endeavor and questions both the wisdom and necessity of doing so. Regulation A was a flawed exemption at its inception. With its Regulation A revival, the J.O.B.S. Act has only succeeded in sparking debate from regulators and politicians, neither of whom have likely taken the time to critically assess the situation. If they had, they would have come to the same conclusion: *let a sleeping regulation lie*. Regulation A was well on its way to extinction. As will be discussed later in this paper, there was only one qualified Regulation A offering in 2011. This is compared to 8,194 Regulation D offerings where the offering size was $5 million or less.[20] Congress should have left Regulation A alone and let it continue to be phased out of use altogether.

B. *Title IV – Small Company Capital Formation*

As mentioned earlier, Title IV revises Regulation A with the intent of making it more appealing to issuers.[21] The most significant Regulation A modification was the increased cap on its offering size. The J.O.B.S. Act raised the Regulation A offering limit from $5 million to $50 million.[22] Additionally, Title IV has enacted counteracting modifications to offset the

18. For example, Rule 506 of Regulation D is the most often used Private offering exemption for reasons that will be explained later in this paper. 17 C.F.R. § 230.506 (2015). *See also* U.S. GOV'T ACCOUNTABILITY OFFICE, GAO-12-839, SECURITIES REGULATION: FACTORS THAT MAY AFFECT TRENDS IN REGULATION A OFFERINGS (2012), at 10-11 (Report details how issuers choose Regulation D's Rule 506 with much more frequency than Regulation A).

19. Samuel S. Guzik, *Regulation A+: A Sleeping Giant For Small Business Capital Formation?*, CROWDFUND INSIDER (Apr. 28, 2014, 8:00 AM), http://www.crowdfundinsider.com/2014/04/37035-regulation-sleeping-giant-small-business-capital-formation/, *archived at* http://perma.cc/CDY9-3PJZ.

20. U.S. GOV'T ACCOUNTABILITY OFFICE, GAO-12-839, SECURITIES REGULATION: FACTORS THAT MAY AFFECT TRENDS IN REGULATION A OFFERINGS (2012), at 11.

21. *See* Shelby, *supra* note 8, at 25-26.

22. 15 U.S.C. § 77c(b)(2)(A) (2012) ("The aggregate offering amount of all securities offered and sold within the prior 12-month period in reliance on the exemption added in accordance with this paragraph shall not exceed $50,000,000.").

increased exposure to investors as a result of raising its cap.[23] The problems with this and the futility of these modifications will also be discussed in depth throughout the remainder of this article.

II. REGULATION A'S CUMBERSOME ASPECTS – (PRE J.O.B.S. ACT)

Historically, Regulation A was not used frequently. From a compliance standpoint, Regulation A was cumbersome and the most you could raise through the offering was $5 million. Those aspects made Regulation A an exemption with little appeal.[24] A discussion of those cumbersome Regulation A aspects follows.

A. *The Federal Component*

An issuer wishing to file under Regulation A must first file an offering statement referred to as a Form 1-A.[25] This form consists of thirty-five pages of requested information, including business information, financial information, risk factors, use of proceeds, principal stockholders, etc.[26] Securities professionals often compared the Form 1-A disclosures to a full-blown registration statement.[27] The required disclosures are very similar in terms of the breadth and depth of required information. Once all the required disclosures have been provided, a well prepared Form 1-A requires twenty-five to thirty-five pages of disclosed information.[28] Even

23. For example, where the issuer's offering size exceeds $20 million, the issuer must include audited financial statements in the offering circular Regulation A Offering Statement under the Securities Act of 1933, Form 1-A. 17 C.F.R. § 239.90 (2015). *See* 17 C.F.R. § 230.252(a) (2015)(prescribing the informational filing and disclosure requirements for Regulation A offerings); 17 C.F.R. § 239.90 (requiring the use of Form 1-A for Regulation A offerings); S.E.C., Form 1-A — Regulation A Offering Statement Under the Securities Act of 1933, pt. F/S(c), https://www.sec.gov/about/forms/form1-a.pdf, *archived at* https://perma.cc/H6QP-GU3Q (requiring audited financial statements for Tier 2 Regulation A offerings).

24. *See* U.S. GOV'T ACCOUNTABILITY OFFICE, GAO-12-839, SECURITIES REGULATION: FACTORS THAT MAY AFFECT TRENDS IN REGULATION A OFFERINGS (2012), at 11 (showing the number of Regulation A filings compared to other exemptions).

25. 17 C.F.R. § 230.251(d)(1)(i) (2014), *amended by* 17 C.F.R. pt. 230 (2015).

26. SEC, Form 1-ASEC33, https://www.sec.gov/about/forms/form1-a.pdf, *archived at* https://perma.cc/H6QP-GU3Q.

27. In drawing upon the author's own experiences as a practitioner spanning from 1998-2003, I never considered Regulation A as a viable option for my clients based in large part on the significant amount of time and expense that would be required to complete the Form–1A Offering Statement.

28. *See, e.g.*, Lightspeed Sys., Inc., Regulation A Offering Statement Under the

though Regulation A technically does not require registration, the issuer must file the Form 1-A with the SEC where it will go through a qualification process.[29] An SEC examiner reviews the document to make sure the disclosures have comported with the Form 1-A's disclosure requirements. When the examiner is satisfied, then the SEC will qualify the offering.[30]

According to a General Accountant's Office (GAO) study, the Regulation A qualification process took an average of 228 days,[31] almost two-thirds of a year. The GAO report (Report) did not offer any explanations as to why the qualification process took so long to complete, but after reviewing over forty Regulation A filings, a plausible answer was evident. Many of the Regulation A filings sampled were prepared without counsel's assistance. This conclusion was based on the fact that these filings were either hand written or written in such a way that it was clear the offering was not drafted by an attorney. Much of the Form 1-A's required disclosures were either inadequate or non-existent in the offering statements that were reviewed. Thus, the likely reason for the extended timeline to qualification was the considerable back and forth between the Commission and the filer to ensure that the filer complied with all of the Form 1-A mandates. Accordingly, if an issuer took the additional steps of hiring accountants and lawyers to assist in preparing the offering statement, this would add considerable expense to a filing process that again, at the most, would yield gross proceeds of $5 million.[32]

B. *The State Component*

In addition to the cumbersome federal component just described, Regulation A has a state registration component as well.[33] Layering the

Securities Act of 1933 (Form 1-A) (June 30, 2008), http://www.sec.gov/Archives/edgar/vprr/08/9999999997-08-030442, *archived at* http://perma.cc/UY3B-7D6C (example of a Form 1-A that contained 121 pages of disclosure filed in 2008 by a company called Lightspeed Systems, Inc.).

29. *See* U.S. GOV'T ACCOUNTABILITY OFFICE, GAO-12-839, SECURITIES REGULATION: FACTORS THAT MAY AFFECT TRENDS IN REGULATION A OFFERINGS (2012), at 11-12 (providing a detailed description of qualification process).

30. 17 C.F.R. § 230.252(g) (2015).

31. *See* U.S. GOV'T ACCOUNTABILITY OFFICE, GAO-12-839, SECURITIES REGULATION: FACTORS THAT MAY AFFECT TRENDS IN REGULATION A OFFERINGS, *supra* note 29, at 12 (according to SEC data obtained covering the periods from 2002–2011).

32. 17 C.F.R. § 230.251(b) (2014) (pre-J.O.B.S. Act) *amended by* 17 C.F.R. pt. 230 (2015).

33. *See generally* 15 U.S.C. § 77r (2012) (exempting under Section 18 of the Securities Act of 1933 certain securities and securities offerings from state registration, but not

state components on top of an already burdensome federal qualification process makes for a regime that has caused many issuers to turn to other options. Under the state registration component, the issuer has to register in each state that the issuer is considering offering its securities.[34] The difficulty here is that each state has its own and often varied registration requirements.[35] To properly register an offering, the issuer has to make sure it complies with the registration process for each state.[36]

To conform, the issuer has to research the registration requirements in each jurisdiction.[37] Adding to the difficulty, each jurisdiction has different filing requirements.[38] Some states merely have a "disclosure" review where the issuer simply comports with the disclosure requirements in that jurisdiction.[39] But some states also have a "merit review" where the state regulator not only reviews the issuer for adequate disclosure but also makes a merit assessment.[40] These merit reviews take such forms as not passing on the filing if the issuer does not show positive earnings within the three years preceding the offering.[41] The combined weight of the cumbersome federal qualification requirement and the numerous state registration requirements is more than enough to push Regulation A down and ultimately off the list of exempt transaction possibilities.

III. REGULATION A AND ITS LACK OF HISTORICAL USE

Due to all that historically was involved with a Regulation A filing, Regulation A has gone from an exemption that was used sparingly in the early '90's to one that today is close to dormant in relative terms. For example, in 1992 there were only 20 Regulation A filings, of which all 20 were qualified.[42] Regulation A filings peaked around 1997 when issuers

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exempting offerings made under Regulation A (pre-J.O.B.S. Act)).

34. U.S. GOV'T ACCOUNTABILITY OFFICE, GAO-12-839, SECURITIES REGULATION: FACTORS THAT MAY AFFECT TRENDS IN REGULATION A OFFERINGS, *supra* note 29, at 13.

35. *Id*. at 13.

36. *See id*. at 13-14 (describing the two general methods for registering securities offerings in specific states).

37. *But cf*. *id*. at 13-19 (pointing out that state regulators are putting forth the effort to streamline the process).

38. *See id*. at 13-14 (describing the two general methods for registering securities offerings in specific states).

39. *Id*. at 13.

40. *Id*.

41. *Id*. at 14.

42. *See id*. at 9, fig. 1 (showing the number of Regulation A filings between 1992 and 2011 and the Regulation A offerings that were actually qualified during that same period).

filed 116 Regulation A offering circulars.[43] But of the 116 filings, only 56 (roughly half) actually worked their way through the Commission's review process and obtained qualification.[44] By 2011, the Regulation A filing number dwindled to nineteen with the Commission only qualifying one of those nineteen Regulation A filings;[45] numbers never lie. Regulation A with its comprehensive offering circular, coupled with its state filing requirements, presented an option that was cumbersome, time-consuming, and costly and therefore was regularly passed over for other more appealing options.

A. *Comparing Regulation A's Use with Other Exemptions*

In making the argument for the J.O.B.S. Act's futility in revising Regulation A, it is enlightening to look at the other available private exemption options to appreciate what makes the other choices preferable. In the GAO study mentioned earlier, the GAO compared Regulation A's use with other potential exempt offerings. The GAO's results were revealing. The report looked at the period covering the years 2008-2011 and compared Regulation A with Regulation D's Rule 506.[46] Regulation D's Rule 506 is another exempt offering available under the Securities Act which allows issuers to offer securities to private investors without having to register those securities.[47] Under Regulation D's Rule 506, the issuer can transact an exempt offering with no dollar limit.[48] But the investors must either be accredited or have a threshold level of financial sophistication to participate in the offering.[49] Also, the rule requires that financial disclosures be made to those investors who are not accredited investors.[50] Further (*and stated with emphasis*), Rule 506 is exempt from

43. *See id.* at 5-6 (noting that although the issuer that relies on Regulation A is not required to register the securities with the Securities and Exchange Commission, the issuer still must file its Regulation A offering circular with the Commission for review and approval); *see id.* at 6 (noting that once the offering has been approved it is deemed to be "Qualified.").

44. *Id.* at 8.

45. *See id.*, at 9, fig.1 (showing the number of Regulation A filings between 1992 and 2011 and the Regulation A offerings that were actually qualified during that same period).

46. *Id.* at 10-11.

47. *See* 17 C.F.R. § 230.506 (2015) (providing exemption for limited offers and sales without regard to the dollar amount as along as all the other criteria are met, there is no offering limit).

48. *Id.*

49. *Id.* at § 230.506 (b)(2), (c)(2).

50. *See id.* at (b)(1)(stating that the issuer must satisfy the terms and conditions of section 230.501 and section 230.502). Rule 502(b) specifies the financial disclosures that

all state filing and registration requirements.[51] The exemption from the state filing requirements is granted explicitly through Section 18(b)(4)(D) of the Securities Act of 1933.[52] Rule 506 is being used for comparison because it was by far the predominate choice for private placement offerings.[53] The numbers by comparison were staggering.

The GAO Report did not obtain Regulation D numbers for 2008 and 2009. But during those two years, the number of Regulation A offerings that were QUALIFIED were eight and three respectively.[54] In 2010 there were six qualified Regulation A offerings.[55] By comparison, in 2010 there were a total of 7,517 exempt offerings filed under Regulation D's Rule 506.[56] And to achieve the most meaningful comparison possible, the Report only included those Regulation D offerings that were for $5 million or less, the maximum Regulation A offering amount prior to its change to $50 million under the J.O.B.S. Act.[57] Likewise in 2011, there was only one qualified Regulation A offering compared to 8,194 offerings filed under Regulation D's Rule 506 for offering amounts of $5 million or less.[58] Rule 506 is vibrant and often used. Regulation A by comparison has been trending downward since its peak of fifty-seven qualified offerings in 1998.[59]

the issuer must provide to certain investors; namely non-accredited investors. 17 C.F.R. § 230.502(b) (2015). Generally, the larger the offering, the more financial and non-financial information the issuer is required to provide to its investors. *Id*.

51. *See* 15 U.S.C. § 77r(b)(4)(D) (2012) (exempting offerings issued under section 4(a)(2) of the Securities Act of 1933 (codified at 17 U.S.C.§ 77d(2) (2012)). Regulation D Rule 506 is a Regulation issued under section 4(a)(2) of the Securities Act of 1933 and is therefore exempt. *See* 15 U.S.C. § 77r(b)(4)(E) (2012).

52. *See* 15 U.S.C. § 77r(b)(4)(D) (2012) (exempting offerings issued under section 4(a)(2) of the Securities Act of 1933 (codified at 17 U.S.C.§ 77d(2) (2012)). Regulation D Rule 506 is a Regulation issued under section 4(a)(2) of the Securities Act of 1933 and is therefore exempt. *See* 15 U.S.C. § 77r(b)(4)(E) (2012).

53. U.S. GOV'T ACCOUNTABILITY OFFICE, GAO-12-839, SECURITIES REGULATION: FACTORS THAT MAY AFFECT TRENDS IN REGULATION A OFFERINGS (2012), *supra* note 29, at 10.

54. *Id*. at 11, tbl. 1.

55. *Id*.

56. *Id*.

57. *Id*. at 10, 11 tbl. 1.

58. *Id*. at 11 tbl.1. Regulation D's Rule 506 places no limits on the offering amount. 17 C.F.R. § 230.506 (2015). Therefore, the GAO Report only used the Rule 506 offerings that were for $5 million or less. U.S. GOV'T ACCOUNTABILITY OFFICE, GAO-12-839, SECURITIES REGULATION: FACTORS THAT MAY AFFECT TRENDS IN REGULATION A OFFERINGS (2012), *supra* note 29, at 10, 11 tbl.1.

59. U.S. GOV'T ACCOUNTABILITY OFFICE, GAO-12-839, SECURITIES REGULATION: FACTORS THAT MAY AFFECT TRENDS IN REGULATION A OFFERINGS (2012), *supra* note 29, at 9 fig.1.

B. *Why Regulation D's Rule 506 is the Preferred Choice*

When comparing the Rule 506 requirements to Regulation A, it is clear why Rule 506 has been the preferred choice.

OFFERING SIZE – Prior to the J.O.B.S. Act, Regulation A's offering size was capped at $5 million;[60] whereas under Rule 506, there is no offering size limit.[61] Issuers can do an offering of any size, as long as the Rule 506 requirements are met. But as highlighted earlier, issuers overwhelmingly chose Rule 506 over Regulation D even where the offering sizes were less than $5 million.[62]

DISCLOSURE REQUIREMENTS – Rule 506 has no disclosure requirements for offerings made to accredited investors.[63] However, the rule does require that audited financial statements be furnished to investors that are not accredited.[64] Where disclosure is required, the depth and breadth of financial disclosure required depends on the offering size.[65] Generally speaking, as the offering size gets bigger, the depth and breadth of financial disclosure under Rule 506 increases.[66] By comparison, Regulation A requires the issuer to prepare and file the thirty-five page Form 1-A regardless of whether the investors are accredited or not.[67] In this regard, the disclosure requirements for Rule 506 and Regulation A are comparable. But the significant difference is that the Regulation A exemption requires the issuer to file the offering statement with the SEC and be subject to SEC review and qualification.[68] Rule 506 merely requires

60. 17 C.F.R. § 230.251(b) (2014) (specifying $5 million limit) (amended by 17 C.F.R. pt. 230 (2015)).

61. 17 C.F.R. § 230.506 (2015). Whereas Rule 504 and 505 specify limits of $1 million and $5 million respectively, Rule 506 does not state any dollar limit. 17 C.F.R. §§ 230.504-.506 (2015).

62. U.S. GOV'T ACCOUNTABILITY OFFICE, GAO-12-839, SECURITIES REGULATION: FACTORS THAT MAY AFFECT TRENDS IN REGULATION A OFFERINGS (2012), *supra* note 29, at 11 tbl.1.

63. *Cf*. 17 C.F.R. § 230.502(b)(1) (2015) (recommending that disclosures be made to accredited investors to avoid running afoul of the anti-fraud provisions under both the '33 and '34 Acts.).

64. *Id*. at §230.502(b)(1)-(2).

65. *See id*. at § 230.502(b)(2)(ii)(B)(1) (requiring an audited balance sheet dated within 120 days from the issued date for offerings up to $2,000,000); *see id*. § 230.502(b)(2)(ii)(B)(2) (requiring additional disclosures such as audited financial statements for a specified number of years for offerings up to $ 7,500,000). *See id*. § 230.502(b) (2015) (listing the full complement of required disclosures).

66. *See id*. at § 230.502(b)(2)(ii)(B) (describing the disclosure requirements for offerings of various sizes).

67. *Id*. at § 230.252(a).

68. U.S. GOV'T ACCOUNTABILITY OFFICE, GAO-12-839, SECURITIES REGULATION:

that the disclosure be made directly to the potential investors.[69] This difference is significant in that filing with the SEC results in an average qualification period of 228 days for a Regulation A filing; whereas under Rule 506 such a qualification process does not exist.[70] Therefore there is no wait time involved under a Rule 506 offering. The issuer can offer its securities immediately under a Rule 506 offering.[71]

INVESTOR QUALIFICATIONS – Rule 506 has qualification criteria for its potential investors. Investors must either be accredited, or "sophisticated."[72] By "sophisticated" the Rule states explicitly, "[e]ach purchaser who is not an accredited investor either alone or with his purchaser representative(s) has such knowledge and experience in financial and business matters that he is capable of evaluating the merits and risks of the prospective investment. . . ."[73] By comparison, Regulation A has no qualifying criteria for its investors. Anyone can participate in a Regulation A offering regardless of their net worth, income, or their financial sophistication.[74]

At first blush, the "no investor qualification requirement" under Regulation A may appear to be an advantage and would add to Regulation A's appeal, but a review of some forty-two Regulation A filings between 2008 and 2014 pointed toward a contrary conclusion.[75] This study revealed that even though the issuers were filing under Regulation A, their filing documents indicated either a clear preference for investors that were either accredited out right, or loosely met the accredited investor criteria. Six out

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FACTORS THAT MAY AFFECT TRENDS IN REGULATION A OFFERINGS (2012), *supra* note 29, at summary page *What GAO Found*.

69. *See* 17 C.F.R. § 230.502(b) (2015) (specifying the non-financial and financial information to be disclosed to investors). No SEC filing requirement is stated in the Regulation D except the requirement to file what is referred to as a Form D. 17 C.F.R. § 230.502(c)(2) (2015).

70. U.S. GOV'T ACCOUNTABILITY OFFICE, GAO-12-839, SECURITIES REGULATION: FACTORS THAT MAY AFFECT TRENDS IN REGULATION A OFFERINGS (2012), *supra* note 29, at 12.

71. 17 C.F.R. §§ 230.502, .506 (2015). Rule 502 does require the issuer to file what is called a Form D with the SEC. 17 C.F.R. § 230.502(c)(2) (2015). But this is merely a notice filing requirements and is not subject to an SEC review or qualification process. 17 C.F.R. § 230.502(c)(2) (2015).

72. 17 C.F.R. § 230.506(b)(2)(ii) (2015).

73. *Id*.

74. *See generally* 17 C.F.R. §§ 230.251–.263 (2015) (placing no stipulations on the investor's qualifications and, by inference, allowing anyone to invest in a Regulation A offering regardless of net worth, income, or financial sophistication).

75. 42 Regulation A filings covering 2008-2014 were randomly selected. Each of the 42 filings selected are listed 1-42 in the Appendix: Part A with specific findings broken out into categories in Appendix: Part B.

of the forty-two Regulation A filings reviewed limited their pool of potential investors to accredited investors only.[76] Additionally, ten out of the forty-two filings placed a minimum investment amount of $1,000 or more.[77] Only nine out of the forty-two indicated a clear intent to solicit investors publicly.[78] And only three out of the forty-two filings indicated that they were actively seeking investors without regard for the investor's income, net worth, or financial sophistication.[79] So, where one might initially think Regulation A provides advantages with its more liberal investor qualification criteria, as a practical matter the reality pans out quite differently. The issue of investor qualifications will be explored in more detail later in this paper.

C. *The Onerous State Provisions*

As briefly mentioned earlier, under Regulation D's Rule 506, the issuer is exempt from any State Blue Sky registration requirements.[80] Specifically, this means that the issuer can forego all state registration or filing requirements. By contrast, Regulation A requires registration in each state where the issuer is going to be offering securities.[81] This state component adds significant effort on the issuer's part as the issuer must research each state's individual registration requirements and then the issuer must tailor its filing to comport with each state.

When looking at all that is required, it is clear why Regulation A historically has not been the exemption of choice; too much required for too little benefit. But Congress has concluded incorrectly that if it simply makes some "tweaks" to Regulation A, the tweaks will make Regulation A a more viable option and issuers will select the Regulation A exemption with more frequency than what has occurred historically.[82] But Regulation

76. *See infra* Appendix: Part B, Category 1 which lists the Regulation A filers that limited their pool of investors to accredited investors only.

77. *See infra* Appendix: Part B, Category 4 for a list of Regulation A filers stipulating at least a $1,000 per investor minimum.

78. *See infra* Appendix: Part B, Category 6 for a list of Regulation A filers who showed a clear intent to solicit investor publicly.

79. *See infra* Appendix: Part B, Category 7 for a list of Regulation A filers that clearly indicated through a low per share purchase price and no investor criteria that their offering was open to any interested investor.

80. 15 U.S.C. § 77r(b)(4)(E) (2012).

81. U.S. GOV'T ACCOUNTABILITY OFFICE, GAO-12-839, SECURITIES REGULATION: FACTORS THAT MAY AFFECT TRENDS IN REGULATION A OFFERINGS (2012), *supra* note 29, at 13.

82. *Spurring Job Growth Through Capital Formation While Protecting Investors—Part I: Hearing Before the Comm. on Banking, Hous., & Urban Affairs*, 112th Cong. 25-26

A was a flawed exemption from its inception and any changes to it won't be enough. The fact that there are other choices that do everything that Regulation A does but with much less burden makes Regulation A a "non-starter" even with the revisions that have been proposed under the J.O.B.S. Act.[83] Those revisions will be discussed and analyzed in the following section.

IV. THE J.O.B.S. ACT'S REGULATION A MODIFICATIONS

On March 25, 2015, after much political wrangling, the SEC, in a rare act of defiance against state regulators, drafted final rules to amend Regulation A.[84] The highlights to the SEC's final Regulation A rules are as follows:

A TWO-TIERED OFFERING SYSTEM: In the SEC's final rules, it has divided Regulation A offerings into two tiers: Tier 1 and Tier 2.[85] Tier 1 is for offerings up to $20 million.[86] Tier 2 is for offerings between $20 million and $50 million.[87] The SEC's final rules have different filing, reporting, and disclosure requirements for each of the two tiers.

TIER 1 – Tier 1 relates to offerings up to $20 million.[88] Under the Tier 1 Regulation A offering regime, the issuer's maximum offering amount can be up to, but may not exceed, $20 million.[89] Under the Tier 1 offering regime, the investors need not have any special investor qualifications;[90] the investors can be both accredited and non-accredited investors and there is no limit as to how much any one investor can invest.[91] Under the Tier 1

(2011) (inquiry from Sen. Richard Shelby, Ranking Member, Comm. on Banking, Hous., & Urban Affairs), http://www.gpo.gov/fdsys/pkg/CHRG-112shrg74738/html/CHRG-112shrg74738.htm, *archived at* http://perma.cc/2G6S-JMU6. Legislative hearings testimony suggests that simply raising the dollar limit on Regulation A and making other modifications will fix what has been ailing the Regulation A exemption since its inception.

83. As discussed previously, Regulation D's Rule 506 has no dollar limit and the issuer is preempted from state registration requirements. 17 C.F.R. § 230.506 (2015). *See generally* 15 U.S.C. § 77r (2012) (exempting under Section 18 of the Securities Act of 1933 certain securities and securities offerings from state registration, but not exempting offerings made under Regulation A (pre-J.O.B.S. Act)).

84. Amendments for Small and Additional Issues Exemptions Under the Securities Act (Regulation A), 80 Fed. Reg. 21806 (Apr. 20, 2015) (to be codified at 17 C.F.R. pts. 200, 230, 232, 239, 240, 249, and 260).

85. 17 C.F.R. § 230.251(a) (2015).

86. *Id*. at § 230.251(a)(1).

87. *Id*. at § 230.251(a)(2).

88. *Id*. at § 230.251(a)(1).

89. *Id*.

90. *Id*.

91. *See id*. (imposing no specific requirements for the investor's qualifications and no

offering regime, the issuer can widely solicit investors, and the shares come with no restrictions on resale.[92]

Under the Tier 1 regime, the issuer will be required to complete the same qualification process as mentioned earlier with the filing of Form 1-A.[93] Consistent with the Regulation A requirements prior to the J.O.B.S. Act, the Issuer need not include audited financial statements with the filing.[94] Likewise, the issuer will not be subject to ongoing periodic financial disclosures or reporting requirements.[95] Under the Tier 1 offering regime, the issuer will remain subject to state filing and registration requirements.[96] In sum, all Tier 1 offerings will be subject to the same requirements that were in place prior to the J.O.B.S. Act. No changes were made to the previous Regulation A provisions other than raising the cap from $5 million to $20 million.[97]

TIER 2 — Under the Tier 2 Regulation A offering regime, the issuer can offer securities for amounts between $20 million and $50 million.[98] Similar to Tier 1 investors, Tier 2 investors need not have any special investor qualifications.[99] But, non-accredited investors may not invest more than 10% of either their annual gross income or 10% of their net worth, whichever is greater.[100] Again, similar to Tier 1, Tier 2 issuers can advertise for and solicit investors.[101]

The filing and reporting requirements, however, are much more stringent for Tier 2 issuers. Under Tier 2, the issuer must include audited financial statements with its Form 1-A offering statement.[102] Additionally,

limits on the amounts of investments).

92. *Id. at* § 230.255(a).

93. *Id.* at § 230.252(a).

94. *Id.*

95. *Id.* at § 230.257(a).

96. 15 U.S.C. § 77r(b)(4) (2012) (comparing Section 15 to Section 18 to show that Section 18 of the Securities Act of 1933 generally does not exempt Regulation A offerings from state registration and filing requirements).

97. *Compare* 17 C.F.R. § 230 (2015), *with* 17 C.F.R. § 230 (2014) (as amended by 17 C.F.R pt. 230 (2015)) (showing no changes other than the raising of the cap).

98. 17 C.F.R. § 230.251(a)(2) (2015).

99. *See id.* (containing no requirements for special investor qualifications).

100. *Id.* at § 230.251(d)(2)(i)(C).

101. *Id.* at § 230.255.

102. Regulation A Offering Statement under the Securities Act of 1933, Form 1-A, 17 C.F.R. § 239.90 (2015) prescribes the informational filing and disclosure requirements for Regulation A offerings. 17 C.F.R. § 230.252(a) (2015). *See* 17 C.F.R. § 239.90 (requiring the use of Form 1-A for Regulation A offerings); S.E.C., Form 1-A — Regulation A Offering Statement Under the Securities Act of 1933, pt. F/S(c), https://www.sec.gov/about/forms/form1-a.pdf, *archived at* https://perma.cc/H6QP-GU3Q (requiring audited financial statements for Tier 2 Regulation A offerings).

the issuer must prepare and file annual, semi-annual, and current financial reports with the SEC.[103] These reports must include audited financial statements.[104] There is an important caveat to the ongoing financial reporting requirement. The issuer's Tier 2 reporting obligations will be suspended if the issuer has less than 300 shareholders.[105] This suspension applies only after the issuer completes all of its reporting obligations during the year in which the SEC qualifies the offering statement.[106] Finally and most significantly, Tier 2 offerings are exempt from all state filing and registration requirements.[107]

Not surprisingly, the NASAA, as a body comprised of state securities regulators,[108] was strongly opposed to state preemption. State preemption divests state securities regulators involvement from all Tier 2 offerings. Their general position is that, without the state registration requirement, investors in their jurisdictions would be exposed to fraud and would be taken advantage of.[109] They also expressed the feeling that they, as state regulators, were closer to any local situation and were therefore in a better position to oversee securities offerings occurring within their borders.[110] The legal fallout surrounding the SEC's final controversial Regulation A rules will be discussed in depth in Section VI.

103. 17 C.F.R. § 230.257(b) (2015).

104. *Id.* at § 230.257(b)(2)(i)(A).

105. *Id.* at § 230.257(d)(2).

106. *Id.*

107. 15 U.S.C. § 77r(b)(3) (exempting sales of securities to "qualified purchasers," as defined by SEC rules, from state regulation of securities offerings). Regulation A's final rules broadly define "qualified purchaser" as "any person to whom securities are offered or sold pursuant to a Tier 2 offering of this Regulation A." 17 C.F.R. § 230.256 (2015).

108. North American Securities Administrators Association (NASAA) is an international organization of security administrators devoted to investors protection. *About us*, N. AM. SEC. ADM'RS ASS'N, http://www.nasaa.org/about-us/, *archived at* http://perma.cc/BS59-KUBC (last visited Nov. 29, 2015). In the United States, NASAA is "the voice of state and provincial securities regulators." *Id.* NASAA's jurisdiction extends to "a wide variety of issuers and intermediaries who offer and sell securities to the public." *Id.*

109. *See, e.g.*, Andrea Seidt, President, N. Am. Sec. Adm'rs Ass'n, Inc., Comment Letter in Response to the Proposed Rule Amendments for Small and Additional Issues Exemptions Under Section 3(b) of the Securities Act at 10, 14 (Mar. 24, 2014), http://www.sec.gov/comments/s7-11-13/s71113-75.pdf, *archived at* http://perma.cc/G3V4-NP9J (arguing that maintaining state registration of Regulation A offerings will promote investor protections by States as intended by Congress).

110. *See, e.g.*, William M. Beatty, Sec. Adm'r, State of Wash., Dep't of Fin. Insts., Comment Letter in Response to the Proposed Rule Amendments for Small and Additional Issues Exemptions Under Section 3(b) of the Securities Act at 3 (Mar. 24, 2014), http://www.sec.gov/comments/s7-11-13/s71113-76.pdf, *archived at* http://perma.cc/E9MT-T3B3. ("In light of the local nature of these offerings, state regulation of these offerings is essential to investor protection and the facilitation of capital formation").

V. BUT WILL THOSE MODIFICATIONS MAKE A DIFFERENCE?

But will Regulation A, even with its modifications that seek to strike a compromise between capital seekers and state regulators, make the Regulation A private offering exemption a more appealing alternative? The answer is no. To support the "no" conclusion, the best approach is to engage in a speculative exercise. The exercise posits why, in theory, an issuer might choose Regulation A over another viable alternative and then provides rebutting arguments against the position of choosing regulation A over another viable position.

A. *Why Regulation A (in theory)?*

Theoretically speaking, when would an issuer choose Regulation A (as modified) over some other exemption? If the issuer is being thoughtful about the decision, it would choose Regulation A only when the Regulation A exemption provides something or allows for something that other exemptions do not. In that regard, Regulation A has two distinguishing characteristics that are present both before and after its modifications under the J.O.B.S. Act.

First, under Regulation A, the issuer can advertise for and publicly solicit potential investors.[111] Thus, under Regulation A, the issuer can cast a wider net when seeking potential investors. This theoretically allows the issuer to draw from a bigger pool of potential investors and therefore increases the likelihood that the issuer will raise the amount of equity it is seeking from the offering.

Second, Regulation A has no investor qualification criteria.[112] Anyone, regardless of income, net worth, or financial knowledge and sophistication, can participate in a Regulation A offering.[113] In theory, this increases the pool of potential investors that can participate in the issuer's offering. Also, the issuer can target and include selected individuals as investors regardless of their net worth, income, or financial sophistication.

111. 17 C.F.R. § 230.255(a) (2015) ("At any time before the qualification of an offering statement, including before the non-public submission or public filing of such offering statement, an issuer or any person authorized to act on behalf of an issuer may communicate orally or in writing to determine whether there is any interest in a contemplated securities offering.").

112. *See generally* 17 C.F.R. § 230.251-.263 (2015) (imposing no investor requirement criteria). Typically when an offering exemption has investor qualifications or criteria, those qualifications and criteria will be specified in the exemption. Regulation A, consisting of Rules 251-263, makes no mention of investor qualifications or criteria.

113. *Id.*

Thus, a Regulation A offering allows the issuer to include a broader investor pool, one that can include both sophisticated and unsophisticated investors as well as both high- and low-net-worth individuals, whereas under other exemptions, unsophisticated and low net worth investors would be excluded such as under the Regulation D Rule 506 offering exemption.[114] These two distinguishing Regulation A characteristics may, in some circumstances, make Regulation A the preferable choice, at least in theory.

B. *But Why Not Regulation A in Practice?*

But in practice, these perceived Regulation A advantages do not seem to be factors that an issuer considers when deciding to do a private offering under Regulation A. Also, what may seem to be an advantage of being able to draw from a larger pool of "lay investors," upon further examination, is not advantageous at all and is not something that factors heavily into an issuer's decision-making.

i. Regulation A Filers Still Sought Out High Net Worth and High Income Individuals

First off, Title II of the J.O.B.S. Act changed the solicitation rules.[115] Now, under added Regulation D Rule 506(c), issuers can solicit and advertise for investors with the caveat that actual investors must be accredited.[116] Prior to the J.O.B.S. Act, soliciting investors for a Regulation D Rule 506 offering was prohibited.[117] By contrast, Regulation A allows for both public solicitation and places no stipulations on the investor's qualifications.[118] While this is a very real difference in theory, in practice,

114. *Id*. at § 230.506(b)(2)(ii).

115. Jumpstart Our Business Startups Act (J.O.B.S. Act), Pub. L. No. 112-106, § 201(a)(1), 126 Stat. 306, 313 (2012) (codified as amended in scattered sections of 15 U.S.C.) (directing SEC to revise solicitation rules applicable to offers and sales pursuant Rule 506).

116. 17 C.F.R. § 230.506(c) (2015). Rule 506(c) was added pursuant to the J.O.B.S. Act's Title II. J.O.B.S. Act § 201(a)(1).

117. *Compare* 17 C.F.R. § 230.502(c) (2015) (effective Sept. 15, 2008 to Mar. 27, 2012) (amended by Jumpstart Our Business Startups Act (J.O.B.S. Act), Pub. L. No. 112-106, § 201(a)(1), 126 Stat. 306, 313 (2012)) (preventing promotion unless allowed under § 230.504(b)(1) or § 230.506(c)), *with* 17 C.F.R. § 230.502(c) (2013) (Pre-J.O.B.S. Act version, not providing an exception for promotion under the Rule 506(c) provision, which provision allows advertising and solicitation as long as the actual investors are accredited).

118. *See* 17 C.F.R. § 255(a) (2015) (allowing for public solicitation); 17 C.F.R. § 230.251(a) (2015) (imposing no specific requirements for the investor's qualifications and

this perceived Regulation A advantage does not manifest itself in any meaningful way.

The above conclusion is based on a review of forty-two Regulation A filings covering the period from 2008 to 2014.[119] The research found that the perceived advantages related to the more liberal Regulation A public solicitation rules, and the opportunity to cast a wider net to include both accredited and "lay investors," did not bear itself out in practice. In fact, researching these forty-two filings showed that a large majority of the Regulation A filings (some twenty-four percent) likely could have been filed and were perhaps better suited to be filed under a less cumbersome, less expensive, and less time-consuming exemption other than the Regulation A exemption that the issuer chose.[120]

For example, out of the forty-two filings reviewed, six issuers explicitly limited their investor pool to accredited investors (i.e. investors with a net worth greater than $1 million or income in excess of $200,000 in each of the two most recent years) and four issuers limited their investor pool to financially savvy investors.[121] Accordingly, in these instances, whatever benefits that could have been derived from filing under Regulation A such as being open to all investors regardless of income, net worth, or financial sophistication, was negated by the stipulation that the investors either be accredited or be financially savvy; i.e. the requirements for the more often used Rule 506 exemption.[122]

Additionally, at least ten of the filings stipulated that any participating investor had to invest a minimum of $1,000 with one issuer placing a minimum investment at $249,750.[123] Though not an incredibly large amount, the investor minimum again cuts against the grain of being available and open to all investors regardless of income or net worth. Setting a minimum investment amount at $1,000 is still a cap of some significance in that it prevents any "layperson" who does not have at least $1,000 of disposable income available from participating in the offering.

no limits on the amounts of investments).

119. *See infra* Appendix: Part A for the list of forty-two Regulation A filings selected randomly over this period.

120. The twenty-four percent calculation is based on the six Regulation A filings noted infra in Appendix: Part B, Category 1(accredited investors), and Category 2 (sophisticated investors). The investor must meet one of these two criteria to be a qualified investor under Regulation D's Rule 506. *See* 17 C.F.R. § 230.506(b)(2)(ii) (describing the required expertise when a purchaser is unaccredited).

121. *See infra* Appendix: Part B, Categories 1 and 2 for a corresponding explanation.

122. 17 C.F.R. § 230.506 (2015).

123. *See infra* Appendix: Part B, Category 4 which lists the issuers that required an investor minimum of $1,000.

Many in the general population do not have $1,000 or more at their disposal to invest. Placing an investment minimum suggests that the issuers are discriminating somewhat as to the type of investor they are targeting for their offering; yet another aspect that is contrary to what one would expect from Regulation A filers.

ii. Very Few Regulation A Filers Took Advantage of the More Liberal Public Advertising and Solicitation Rules

Recall that Regulation A allows the issuer to publicly solicit investors.[124] Publicly soliciting investors is a practice that was previously prohibited under Regulation D's Rule 506.[125] Thus, if one were being thoughtful about using Regulation A, then you would expect the issuer filing under Regulation A to take advantage of this aspect and cast his net as widely as possible. But only nine filings out of the forty-two stated that their "Plan of Distribution" would involve publicly soliciting investors.[126]

In sum, in the vast majority of the Regulation A filings reviewed, there were perhaps only three issuers that clearly filed under Regulation A because of the distinguishing aspects that Regulation A affords; namely, the ability to publicly solicit investors and the ability to include any and all potential investors regardless of net worth, income, or financial sophistication. All the other Regulation A filers were structured such that they could have filed under Rule 506 and were perhaps better suited for Rule 506 but for some unclear reason they chose the more cumbersome Regulation A path. In the interest of full disclosure, there were at least ten Regulation A filings that were prepared without counsel's assistance.[127] This conclusion was based on the fact that these filings noted either "n/a" or "none" (or some similar indication) where the issuer is asked to indicate whether counsel prepared or assisted in preparing the filing.[128] It is plausible to conclude that these "lay filers" may not have been as familiar with the rules surrounding exempt offerings and the different options each exemption provides. Thus, it is possible that these "lay filers" may have

124. *See* 17 C.F.R. § 230.255 (2015) (describing the requirements that apply when securities are offered in a circular).

125. *See* 17 C.F.R. § 230.502(c) (2013) (Pre-J.O.B.S. Act version of statute, not providing an exception for promotion under the Rule 506(c) provision, which provision allows advertising and solicitation as long as the actual investors are accredited).

126. *See infra* Appendix: Part B, Category 6 for a list of companies giving a clear intent to solicit investors publicly.

127. *See infra* Appendix: Part B, Category 5 for list of issuers who prepared their Regulation A filing without counsel's assistance.

128. *Id.*

chosen an exemption other than Regulation A if they were better informed or had more knowledge about the available choices.

iii. Lay Investors and Low Net Worth or Low Income Individuals Do Not Apply

The takeaway from all of this is clear. Even in the case of the Regulation A filers, issuers seemed to prefer investors that had obtained at least some degree of "financial substance,"[129] either through an accumulated mass of wealth, from earning a solid income, or by otherwise being financially savvy.[130] The reasoning behind this preference is clear, is understandable, and further drives home the point that just because an issuer is able to cast a wider investment net does not mean that it is prudent to do so. Investors who do not have a critical mass of net worth or do not earn an income that allows for a fair amount of disposable income make for a less stable investor pool.

First off, low net worth or low income investors are more likely to be investing money that they can ill afford to lose. Second, investors of this type tend to be a cumbersome lot for the issuer because: (1) they may have a disproportionate amount of money invested in the venture relative to their overall net worth; and (2) they are more likely to be unfamiliar with the speculative nature of investing and the true risks involved. In these instances, the issuer can expect this investor type to be burdensome. It is foreseeable that these unsophisticated investors will make frequent inquiries into how much and when they will get their money back. They may frequently need and require a lot of handholding in terms of explaining what is going on; especially if the issuer's business takes a downturn. In sum, investors of this nature can and often are more trouble than they are worth. Thus, if an issuer finds itself in the situation where Regulation A is the only viable option due to the nature of its potential investor pool, then the issuer should reassess whether it should be doing a private securities offering at all.

This discussion drives home the point as to Regulation A's limited use. If, in fact, it were the case that your investor pool was neither wealthy nor sophisticated, then you have a tenuous investor pool at best. For these reasons, even where issuers were filing under Regulation A, they nonetheless structured their offerings such that "lay investors" would be

129. *See infra* Appendix: Part B, Categories 1-5 for list of companies that placed SOME kind of investor qualification, or criteria as a pre-cursor to investing – whether that be financial sophistication, income or net worth minimums or a minimum investment amount.

130. *Id.*

excluded, and in many cases, the issuer specifically targeted accredited investors to the exclusion of all others.[131] The end result is, although the issuer filed under Regulation A, those filings more often than not could have been filed under another less cumbersome exemption such as Regulation D's Rule 506.

Why issuers chose to file under Regulation A in spite of not making use of Regulation A's distinguishing characteristics is not clear. The likely reason is that the issuer simply did not have a full grasp of all the exempt offering choices and the distinguishing characteristics of each. Again, it is believed that a lot of these choices to file under Regulation A were done without counsel's assistance or were otherwise ill-advised.

C. *How will the J.O.B.S. Act Modifications Affect the Regulation A Decision?*

In spite of all the political wrangling and the SEC's efforts to appease state regulators, the Regulation A end product has resulted in offering exemptions that are still deficient and still fail to consider the end user. Tier 1 contains all of the same onerous provisions that existed prior to the J.O.B.S. Act's revisions, and the Tier 2 regime adds a layer of financial disclosure and reporting requirements that rivals publicly held company disclosures.[132] Therefore, both the Tier 1 and Tier 2 offering regimes are still weighed down with onerous requirements that will cause most potential issuers to choose other options.

TIER 1 (for offerings up to $20 million) – In essence, the Tier 1 requirements are exactly the same as they were prior to the J.O.B.S. Act with the exception that the offering cap has been raised from $5 million to $20 million.[133] Other than that, the exemption is exactly the same as the pre-J.O.B.S. Act version.[134] Under the Tier 1 requirements, the Regulation

131. *See infra* Appendix: Part B, Category 1 for list of Regulation A filers that limited its investor pool to accredited investors as defined under Regulation D, Rule 506. See 17 C.F.R. § 230.506(b)(2)(ii) (outlining the requirements for an unaccredited investor).

132. *See* Form 1-A, 17 C.F.R. § 239.90 (2015), https://www.sec.gov/about/forms/form1-a.pdf, *archived at* https://perma.cc/H6QP-GU3Q (providing the instructions and form related to the offering statement); 17 C.F.R. §§ 230.251-.252, .257 (2015) (outlining the conditions that, when fulfilled, remove the need to register, and providing the requirements of an offering statement and sales report).

133. *Compare* 17 C.F.R. § 230.251(a)(1) (2015) (limiting Tier 1 prices to a maximum of $20 million), *with* 17 C.F.R. § 230.251(b) (2014) (limiting exemption amount to a maximum of $5 million).

134. *Compare* 17 C.F.R. §§ 230.251(a)(1), .252, .257 (2015), *with* 17 C.F.R. §§ 230.251-.252, .257 (2014) (effective to June 18, 2015) (amended by 17 C.F.R. § 230 (2015)) (stating identical requirements for registration, offering statements, and sales reports).

A aspects that made it undesirable prior to its modifications under the J.O.B.S. Act are still present; namely the lack of state preemption which therefore necessitates the need for the issuer to comport with filing and registration requirements in each jurisdiction in which the issuer is offering securities.

The Tier 1 offering regime structured as it is will result in Regulation A remaining in its current state of dormancy because the large majority of potential Regulation A issuers would be the ones whose offerings' sizes would be for $20 million or less. This is because if the issuer were to offer securities for larger amounts, then more than likely the issuer would be of a size and sophistication where they would choose more desirable and less cumbersome exemptions such as Regulation D's Rule 506.

Again, this conclusion is based on our review of some forty-two Regulation A Filings between 2008 and 2014. Those filings revealed issuers, a majority of whom were lacking in sophistication, as evidenced by the deficient manner in which their Form 1-A offering statements were completed.[135] That, coupled with the very low qualification rate mentioned earlier, suggests that the problems with Regulation A prior to the J.O.B.S. Act will persist as the modifications did not address those problems in any meaningful way, if at all.

TIER 2 – Similarly, with the Tier 2 offering regime, the costs to comply still outweigh the corresponding benefits, even with the offering limit raised to $50 million.[136] This is primarily because once an issuer's infrastructure has reached a size where it is in a position to raise up to $50 million, there are alternatives (again Regulation D's Rule 506) that work much better for the issuer than Regulation A and are much less cumbersome.

As discussed earlier, under the Tier 2 offering regime, the issuer must provide audited financial statements in its filing[137] and must also provide audited financial statements on an annual basis.[138] Accordingly, any issuer choosing to offer securities under Regulation A's Tier 2 regime would have to be a company that has reached a critical mass in terms of size and infrastructure to absorb the costs involved with providing audited financial statements in its filing along with providing annual audited financial statements going forward on an ongoing basis. Looking again to the pool of potential investors, there could be a number of possible scenarios.

135. *See* 17 C.F.R. § 230.506(b)(2)(ii) (outlining the characteristics needed when an investor is unaccredited).
136. 17 C.F.R. § 230.251(a)(2) (2015).
137. 17 C.F.R. §§ 230.252(a), 239.90 (2015).
138. 17 C.F.R. § 230.257(b) (2015).

Again, the only one where Regulation A is the superior choice over other options is the scenario where a significant portion, at least a majority, of the issuer's potential investor pool is "lay investors." Otherwise one of the other exemptions (namely Regulation D's Rule 506) would make for a more logical choice. If this is in fact the case, then it is reasonable to conclude that no individual investor would have a large amount of money to invest because if they did, they would more than likely meet the accredited investor criteria. Your pool of investors would therefore be a considerably large number of "lay investors" with each investor contributing a nominal amount to the total offering.

Though this scenario in theory is possible, again, it is not likely. Individuals with little or no disposable income are few and far between in the realm of private placements. The only clear advantage that Regulation A would have over other options would be to tap into this nearly non-existent pool of "lay investors"; an investment pool that is neither viable, desirable, nor prevalent enough to warrant choosing an exemption specifically tailored for their participation. None of these dynamics would change under the modified Regulation A's two tiered offering regime. Regulation A simply does not reconcile to the realities of the market place.

VI. THE STATE PREEMPTION CONTROVERSY

Further weighing Regulation A down and bolstering the argument for its obsolescence are the current and pending controversies surrounding the Commission's state preemption decision for Tier 2 offerings. As discussed earlier, Regulation A, before its revisions under the J.O.B.S. Act, did not allow for state preemption.[139] Pre J.O.B.S. Act, an issuer had to satisfy the registration requirements in each jurisdiction in which the issuer was offering its securities.[140] Let's appreciate the added regulatory burden that this posed by using a real life Regulation A filing as an example.

Godspell LLC is a limited liability company that filed under Regulation A in February of 2010 (pre J.O.B.S. Act).[141] According to its

139. *See* 15 U.S.C. § 77r(b)(4) (2012) (not including Regulation A offerings among offerings that are exempt from state registration and filing requirements).

140. *See* U.S. Gov't Accountability Office, GAO-12-839, Securities Regulation: Factors That May Affect Trends in Regulation A Offerings 8 (2012) (describing how pre-sale registration of an offering is required under state law). Again, this was required because there was no state preemption under the federal securities law for Regulation A offerings. *See* 15 U.S.C. § 77r(b)(4) (2012) (excluding Regulation A offerings from available exemptions).

141. The Godspell LLC, Regulation A Offering Statement Under the Securities Act of 1933 (Form 1-A) (Feb. 23, 2010), http://www.sec.gov/Archives/edgar/vprr/10/9999999997-

Form 1-A offering Circular as of 1/31/2010, Godspell had total assets of $100 and no liabilities.[142] According to its filing documents, Godspell LLC was planning on offering securities in California, Connecticut, Illinois, Louisiana, Massachusetts, Michigan, New Jersey, and New York.[143] Accordingly, in addition to filing its Form 1-A at the federal level, Godspell LLC then had to research and comply with each of the registration requirements in California, Connecticut, Illinois, Louisiana, Massachusetts, Michigan, New Jersey, and New York respectively.[144] These added burdens required additional layers of expense, company resources, and perhaps the most precious commodity of all—time. Pre J.O.B.S. Act, choosing a different exemption meant avoiding all of these registration and compliance hurdles. Because of this, many issuers assessed all that would be involved in doing a Regulation A filing and then ultimately chose to go in a different direction because the cost to comply far outweighed the benefits. The historically low use of Regulation A corroborates this conclusion.[145]

As discussed earlier, the Commission's final rules did in fact preempt state filing requirements for all Tier 2 offerings (i.e. amounts between $20 million and $50 million).[146] But, as expected, state regulators in two jurisdictions have filed suit in reaction to the state preemption decision for Tier 2 offerings, and there are likely to be additional suits to follow.[147] The legal challenges to Regulation A will be discussed in Part B of this section.[148] Accordingly, the fight and the arguments loom, casting a long shadow over those who might choose to venture down the now murky Regulation A path.[149]

10-001230, *archived at* https://perma.cc/LE2T-3PXA.

142. *Id.*

143. *Id.*

144. *Id.* at 50.

145. U.S. Gov't Accountability Office, GAO-12-839, Securities Regulation: Factors That May Affect Trends in Regulation A Offerings (2012), at 9, Figure 1. The Report conveys Regulation A's declining use which peaked at 116 filings in 1997 and has declined steadily through 2011 where there were only 19 Regulation A filings in 2011.

146. Under 15 U.S.C. § 77r(b)(3) sales of securities to "qualified purchasers," as defined by SEC rules, are exempt from state regulation of securities offerings. 15 U.S.C. §77r(b)(3)(2012). Regulation A's final rules broadly define "qualified purchaser" as "any person to whom securities are offered or sold pursuant to a Tier 2 offering." 17 C.F.R. § 230.256 (2015).

147. *Lindeen v. SEC*, No. 15-1149 (D.C. Cir. filed May 22, 2015) and *Galvin v. S.E.C.*, No. 15-1150 (D.C. Cir. filed May 22, 2015) (cases consolidated May 27, 2015).

148. *See supra* Part IV-B (discussing the legal challenges to Regulation A).

149. *See* 17 C.F.R. § 230 (2015) (detailing the stipulations of Regulation A).

A. *The General Arguments Against State Preemption*

Opposition against state preemption, not surprisingly, is strongest with the state regulators, those entities that would be undertaking the task of approving the application for any company seeking to issue securities in that particular jurisdiction. The arguments from those opposing state preemption essentially boil down to positions such as: "[state preemption] would handicap the states from providing oversight . . . at a time when the Commission lacks the resources to police this area."[150] "Regulation A securities can be *high-risk offerings that may also be susceptible to fraud, making protections provided by the State regulators an essential [feature*]."[151] "State regulators are more accountable to local investors and businesses and have the ability to respond quickly to fraudulent offerings occurring in their own backyards."[152]

These arguments are valid, quite valid in fact, but there is a major flaw in their reasoning. These opposing voices fail to consider the issue in its broader context. Yes, it is reasonable to conclude that an additional state regulatory component would likely result in fewer instances of investors being defrauded. But to what end? When you read the comment letters from the state regulators, they do make compelling arguments in projecting dire outcomes for investors if they (the state regulators) are not allowed to inject themselves into the registration process to champion the small investors' cause. But without exception, what is glaringly absent from all of their recriminations is the effect that the state registration requirement will have on Regulation A's actual use. That part of the argument is absent from their protests. It is absent because if these state regulators included or even considered the practical side of the argument, they would have to concede that the state registration requirement bogs down an already overly burdened private offering exemption. Nonetheless, the Commission has acquiesced somewhat to their pleas by keeping the state filing requirements

150. Comment Letter from William M. Beatty, Sec. Adm'r, State of Wash., Dep't of Fin. Insts. Sec. Div., to Elizabeth M. Murphy, Sec'y, SEC, at 1 (Mar. 24, 2014), http://www.sec.gov/comments/s7-11-13/s71113-76.pdf, *archived at* http://perma.cc/E9MT-T3B3.

151. Comment Letter from William M. Beatty, Sec. Adm'r, State of Wash., Dep't of Fin. Insts. Sec. Div., to Elizabeth M. Murphy, Sec'y, SEC, at 2 (Mar. 24, 2014), http://www.sec.gov/comments/s7-11-13/s71113-76.pdf, *archived at* http://perma.cc/E9MT-T3B3 (quoting 157 Cong. Rec. H7, 229-01(daily ed. Nov. 2, 2011) (statement of Rep. Peters)).

152. Comment Letter from William M. Beatty, Sec. Adm'r, State of Wash., Dep't of Fin. Insts. Sec. Div., to Elizabeth M. Murphy, Sec'y, SEC, at 4 (Mar. 24, 2014), http://www.sec.gov/comments/s7-11-13/s71113-76.pdf, *archived at* http://perma.cc/E9MT-T3B3.

for Tier 1 offerings which, as discussed earlier, is a mistake.

Additionally, proponents for the state registration requirement will point to Regulation D Rule 506 and the apparent high incidents of investor fraud as another argument as to why Regulation A should not be similarly exposed.[153] In response to that argument, all laws have their limits. It is hard to legislate people into doing the right thing. Laws designed to protect investors, just like all other laws, have to strike a balance between (in this case) protecting investors while creating a regulatory regime that is worthy from a cost-benefit standpoint. To their credit, at least with respect to Regulation A's Tier 2 offerings, the Commission decided to take a stand in defiance of the state regulators.

B. *State Preemption and the Question of Legality*

Although the SEC has made its final decision regarding state preemption, early signs indicate that State regulators plan to fight the SEC through the courts on the state preemption issue. William F. Galvin, the secretary of the Commonwealth of Massachusetts, has joined Monica Lindeen, Montana State Auditor *ex officio* Montana Commissioner of Securities and Insurance, to consolidate their suit; they have filed a *Petitioners' Preliminary Statement of Issues* against the SEC, contesting state preemption's legality in the absence of what they feel is the express statutory and legal authority to do so.[154]

The *Preliminary Statement of Issues* sets out 4 key issues or questions for the court to address.

> 1. Whether the Commission's adoption of the rule—which defines "qualified purchaser" to mean "any person to whom securities are offered or sold pursuant to a Tier 2 offering under Regulation A—is arbitrary and capricious, an abuse of discretion, or otherwise is unlawful because it conflicts with the plain language of Title IV of the J.O.B.S. Act and Section 18(b)(3) of the Securities Act . . . .

153. *See* Informed Investor Advisory: Private Placement Offerings—Are You an Informed Investor?, N. Am. Sec. Adm'rs Ass'n, http://www.nasaa.org/22284/informed-investor-alert-private-placement-offerings/, *archived at* http://perma.cc/C72Y-E6Y2 (last updated Sept. 2013) (detailing what an investor should know about Regulation D, Rule 506, including that fraud is more likely for Regulation D offerings because of the lack of regulatory review).

154. Petitioners' Joint Preliminary Statement of Issues, *Lindeen v. S.E.C.*, No. 15-1149 (D.C. Cir. filed May 22, 2015) (consolidated with Galvin v. S.E.C., No. 15-1150 (D.C. Cir. filed May 22, 2015)).

> 2. Whether the Commission Violated Sections 2(b), 3(b)(2)(G), and 18(b)(3) of the Securities Act and Section 3(f) of the Securities Exchange Act by preempting state registration and qualification laws in a manner that is inconsistent with the public interest and the protection of investors.
>
> 3.Whether the Commission violated § 2(b) of the Securities Act and Section 3(f) of the Securities Exchange Act by failing to adequately consider the protection of investors and the public interest, among other factors, prior to its adoption of the rule.
>
> 4.Whether the Commission otherwise acted in a manner that is arbitrary and capricious, an abuse of discretion, or otherwise unlawful within the meaning of the Administrative Procedure Act, 5 U.S.C. §§ 701 *et seq*., or other applicable law in adopting its amendments and revisions to Regulation A's exemption from state registration and qualification laws under the Securities Act.[155]

As of the date of this writing, the suit was still in its pleading stages, so the regulators' respective arguments were unavailable prior to this article's publishing. The suit, however, is likely to follow the arguments the NASAA put forth when Regulation A's final rules were still pending and the Commission was still inviting comment letters on the proposed rules.[156]

The NASAA's argument gets its traction from the 1933 Act's Section 18.[157] Section 18 says that state law shall not govern "covered securities."[158] Section 18 goes on further to define a "covered security" as (among other things) "sales to qualified purchasers."[159] Section 18 gives the Commission the authority to define a "qualified purchaser" with the stipulation that any definition must be "consistent with the public interest and the protection of investors."[160]

The Commission has used its rulemaking authority granted under Section 18 to define a "qualified purchaser" simply as one who invests in a

155. *Id*. at 2-3.
156. Comment Letter from Andrea Seidt, President, N. Am. Sec. Adm'rs Ass'n, Inc., to Elizabeth M. Murphy, Sec'y, SEC, at 2-4 (Mar. 24, 2014), http://www.sec.gov/comments/s7-11-13/s71113-75.pdf, *archived at* http://perma.cc/G3V4-NP9J.
157. 15 U.S.C. § 77r (2012) (Exemption From State Securities Regulation Offerings).
158. 15 U.S.C. §§ 77r(a)(1), (2) (2012).
159. 15 U.S.C. § 77r(b)(3) (2012).
160. *Id*.

Tier 2 Regulation A offering.[161] The NASAA, in its comment letter to the Commission, attacked this definition as it applies to Regulation A, noting that an investor in a Tier 2 Regulation A offering should not be defined as a "qualified purchaser."[162] They argue that to do so would be inconsistent with the public interest and the protection of investors.[163]

Unlike Regulation D's Rule 506, Regulation A does not place any restrictions on who can invest in a Regulation A offering. Under Rule 506, investors are restricted to investors who are either accredited or have "*knowledge and experience in financial and business matters that [they are] capable of evaluating the merits and risks of the prospective investment* . . . ."[164], while anyone can invest in a Regulation A offering regardless of accredited investor status or investor sophistication.[165] The NASAA's argument then is simply that defining a Regulation A offeree as a "qualified purchaser" would be misplaced and inappropriate because the potential Regulation A investor could be one who lacks the financial acumen and sophistication to fend for himself.[166] It is likely that any lawsuits filed opposing the Commissions' definition of "qualified purchaser" will have arguments similar to the NASAA's.

The NASAA's argument has merit. As Regulation A is written, the Regulation A investor could be an individual with no financial sophistication whatsoever.[167] The NASAA and the state regulators in its association believe this issue is clear cut and unequivocal, but the matter contains much more nuance where reasonable minds could differ.

The legality of defining a Regulation A investor as a "qualified purchaser" is a matter of judgment, and yes, a matter of statutory interpretation as to whether the Commission is over stepping its rulemaking authority granted under Section 18. Section 18 clearly states that the Commission has the authority to define a "qualified purchaser" but requires the Commission's definition to be "consistent with the public interest and

161. 17 C.F.R. § 230.256 (2015).

162. Comment Letter from Andrea Seidt, President, N. Am. Sec. Adm'rs Ass'n, Inc., to Elizabeth M. Murphy, Sec'y, SEC, at 2-4 (Mar. 24, 2014), http://www.sec.gov/comments/s7-11-13/s71113-75.pdf, *archived at* http://perma.cc/G3V4-NP9J.

163. *Id*. at 2 (emphasis added).

164. 17 C.F.R. § 230.506(b)(2)(ii) (2015).

165. Again, a review of Regulation A reveals no stated qualification criteria for its investors.

166. Comment Letter from Andrea Seidt, President, N. Am. Sec. Adm'rs Ass'n, Inc., to Elizabeth M. Murphy, Sec'y, SEC, at 8 (Mar. 24, 2014), http://www.sec.gov/comments/s7-11-13/s71113-75.pdf, *archived at* http://perma.cc/G3V4-NP9J.

167. *See generally* 17 C.F.R. §§ 230.251-.263 (2015) (stipulating the general requirements of an investor under Regulation A).

the protection of investors."[168] To conclude that the Commission is overreaching in this case, the fact finder must conclude that defining a "qualified purchaser" as one who invests in an exempt offering under Regulation A is inconsistent with the public interest and the protection of investors. How is such a determination made? This assessment is based strictly on the rule maker's (the SEC in this case) judgment.

Rulemaking can never be stated in absolutes. A good rule is one that is written with feasibility and practicality considerations. What good is an exemption that provides the ultimate investor protection but is too burdensome and cost prohibitive to be a viable alternative? Accordingly, both feasibility and practicality considerations should be scrutinized when analyzing the government's intent behind Regulation A. To define Regulation A's Tier 2 offerees and investors as "*qualified purchasers*" would be the Commission making the same practical considerations as it did when it drafted some aspects of Regulation D. Very few rules can be written with absolutes. The drafter almost always has to make some concessions for practical considerations and (in this case) the rule must strike the right balance between protecting investors and keeping the exemption as one that remains viable from a cost-benefit standpoint.

The following example illustrates how concessions are made during the drafting process. In drafting Regulation D, the Commission made some concessions in deference to practical considerations that can result in certain investors participating in a Rule 506 offering who, in actuality, are persons who probably should not be participants in such offerings. Take for example the "accredited investor" definitions under Regulation D.[169] Under the Rule, you qualify as an accredited investor if your net worth exceeds $1,000,000.[170] By this definition, a hypothetical John Doe, who has never allocated one penny of his earnings towards investing or saving, and who might not know a prospectus from a marketing brochure could qualify as an accredited investor if his winning lottery ticket put his net worth over the one million dollar mark. His million plus winnings could go to a private venture of his choosing and the law would define him as an accredited investor; one for whom no special considerations, protections, or disclosures would be required. Here, with Regulation D, the Commission chose the route of defining "accredited investor" in terms of bright line quantifiable metrics for practical considerations. The bright line definitions give issuers seeking to use the Regulation clear and unequivocal guidance

168. 15 U.S.C. § 77r(b)(3)(2012).

169. 17 C.F.R. § 230.501(a)(2015) (giving various definitions of those persons and entities that fall under the accredited investor definition).

170. 17 C.F.R. § 230.501(a)(5) (2015).

on who falls within the definition. This concession was done for reasons of efficiency and practicality, in spite of the fact that some investors may fall through its fissures. Further, Section 2(b) of the Securities Act of 1933 mandates that rules must also take into consideration matters such as practical considerations that facilitate the formation of capital.[171]

The same practical considerations and judgments need to come into play with the Commission and its Regulation A rulemaking. Yes, it is possible (and likely) that defining a "qualified purchaser" as being a Tier 2 Regulation A investor would result in some investors who shouldn't be in that space. But the rule should be drafted with practical considerations in mind as well. Additionally, as discussed earlier, issuers will be self-selecting. Regulation A filers will more than likely seek out either accredited or sophisticated investors and will leave the unenlightened alone.

Additionally, in the proposed rule itself, the Commission also believes that, "substantial investor protections embedded in the issuer eligibility conditions, limitations on investment, disclosure requirements, qualification process and ongoing reporting requirements . . . could address potential concerns that may arise as a result of the preemption of state securities law registration and qualification requirements."[172] Also let's not lose sight of the fact that the provisions of Section 12(a)(2) apply so the investor will always have legal remedies under the law available after the fact.[173] Some may say prevention before the harm occurs is better than trying to remedy a harm after the fact.

Again I respond with the mantra that practical considerations necessitate some acquiescence and compromise in the rulemaking. In this case, foregoing the state registration requirement for Tier 2 issuers is one of those practical considerations and the legality of such action should be upheld. That is if Regulation A has any chance of being viable at all.

In sum, given the uncertainty, and the pending and future litigation

171. 15 U.S.C. § 77b (2012) ("Whenever pursuant to this subchapter the Commission is engaged in rulemaking and is required to consider or determine whether an action is necessary or appropriate in the public interest, the Commission shall also consider, in addition to the protection of investors, whether the action will promote efficiency, competition, and capital formation.").

172. Small and Additional Issues Exemptions Under Section 3(b) of the Securities Act, 79 Fed. Reg. 3926, 3969 (proposed Jan. 23, 2014) (to be codified at 17 C.F.R. pt. 230), http://www.gpo.gov/fdsys/pkg/FR-2014-01-23/pdf/2013-30508.pdf, *archived at* http://perma.cc/EGF3-NL3Y.

173. Section 12(a)(2) of the Securities Act of 1933 grants relief to investors who can show that the prospectus contained a misstatement or an omission if the misstatement or omission were material in nature. 15 U.S.C. § 77l(a)(2) (2012). Section 12(a)(2) essentially grants the relief of refunding the investors' money. *Id.*

that is looming over the Commission's final Regulation A rules, these aspects are additional deterrents to using the Regulation A exemption. The last thing a small business needs is a potential lawsuit related to its exempt securities offering.

C. *The State's Response: A Streamlined Protocol for Regulation A Filings*

To the State's credit, they have made efforts to streamline the state filing and registration requirements. On March 11, 2014, the North American Securities Administration Association announced that its members voted to approve what they describe as a coordinated and more streamlined filing and registration process.[174] The NASAA describes its new "streamlined" review program as follows:

> NASAA has developed streamlined multi-state review protocols for Regulation A and Regulation A+ offerings to ease regulatory compliance costs on small companies seeking to raise capital. Through this program, launched in May 2014, Regulation A filings are made in one place and distributed electronically to all states. Lead examiners will be appointed as the primary point of contact for a filer and each state will be given 10 business days for review. The lead examiners alone will interact with the issuer to resolve any deficiencies.[175]

The new Coordinated Review Program (CRP or Program) is to work as follows. On day one, issuers desiring to avail themselves to this Program will e-mail an electronic copy of its Regulation A filing (the issuer's Form 1-A) along with all accompanying exhibits and such to the State of Washington who will act as the program coordinator.[176] The program coordinator will then distribute these documents to all the states in which the issuer has selected in its application materials.[177] Within three business days after receiving the application materials, the program coordinator is required to select both a disclosure examiner and a lead examiner (assuming registration is sought in both types of jurisdictions). Ten days after the program coordinator selects the lead examiners, the lead

174. N. Am. Sec. Adm'rs Ass'n, NASAA Members Approve Streamlined Multistate Coordinated Review Program (Mar. 11, 2014), http://www.nasaa.org/29699/nasaa-members-approve-streamlined-multi-state-coordinated-review-program/, *archived at* http://perma.cc/3N7E-KHNP.

175. NASAA Multi-state Coordinated Review Program, N. Am. Sec. Adm'rs Ass'n, http://www.nasaa.org/wp-content/uploads/2015/03/Coordinated-Review-Chart.pdf, *archived at* http://perma.cc/5EW3-Y224 (last visited Nov. 29, 2015).

176. *Id*.

177. *Id*.

examiners are required to draft and circulate a proposed comment letter to all the other disclosure and merit states in which the issuer is seeking registration for its offering.[178]

To be clear of what is implied here, the lead examiners have ten days to review the Regulation A filing and prepare a comment letter on issues/deficiencies that the lead examiner surfaces through its review. The lead examiners are then required to circulate that comment letter to all the other participating jurisdictions. Those states then have five additional business days in which to communicate any concerns or comments to the lead examiners.[179] Within three additional business days, the lead examiner is required to make any necessary revisions and then send this initial comment letter to the issuer. "If there are no deficiencies in the application, no comments will be necessary and the registration will be cleared by the lead examiners within 21 business days after it is filed."[180]

"If there are deficiencies, the lead examiners will communicate with the applicant and the participating jurisdictions to resolve deficiencies. Whenever an issuer files a response to any deficiency, the lead examiners will reply within five business days."[181] And this process presumably will repeat itself until the issuer has cleared all the cited deficiencies.

The NASAA states that the new Coordinated Review Program will take a MINIMUM of thirty days.[182] But in looking at the process, in all likelihood it will take much longer than that in most if not all the cases. As discussed and noted earlier, a fair number of these Regulation A filings are prepared without the assistance of counsel. These "issuer prepared filings" are woefully deficient in both their breadth of disclosure and their propriety. It's hard to speculate how long it would actually take to clear the deficiencies with these filings. But if you take the number of Regulation A filings that the SEC qualified between 2008 and 2011 as a basis for comparison, it is reasonable to conclude that the number would be small.[183]

Further, if one has had occasion to prepare a Form 1-A, you would

178. *Id.*
179. *Id.*
180. *Id.*
181. *Id.*
182. Application for Coordinated Review of Regulation A Offering—Form CR-3(b), N. Am. Sec. Adm'rs Ass'n, http://www.nasaa.org/wp-content/uploads/2014/05/Coordinated-Review-Application-Sec-3b.pdf, *archived at* http://perma.cc/ZMX4-XYQL (last visited Nov. 29, 2015).
183. Between 2008 and 2011, the Commission qualified 18 total Regulation A offerings. By comparison, 1289 Registered Public Offerings were filed during that same time period. U.S. Gov't Accountability Office (GAO), Securities Regulation: Factors That May Affect Trends in Regulation A Offerings 11 (July, 2012), supra note 29.

appreciate the voluminous amount of information the issuer is required to furnish. The form alone is twenty-nine pages long before any information is provided.[184] Depending on how exacting the state regulators decide to be, in all likelihood, it could take up to several months to get all the deficiencies cleared. Also, the issuer would be addressing these state level concerns on a parallel track with the Regulation A filing that it completed at the federal level.

In fairness to the state regulators and their proposed program, it will not be known how long the process will actually take unless and until the program is fully implemented and up and running. Regardless of how streamlined the state registration process becomes as a result of the NASAA's changes, with a state component remaining as part of the process, that process will require additional time, effort, and expense from the issuer.

In sum, the NASAA's efforts to streamline the process are commendable. But if the SEC's final rules are somehow overturned for Tier 2 offerings, such a ruling would be yet another anchor weighing down an already encumbered exemption to the point where potential users (who are thoughtful about the decision) will seek a different and less cumbersome exemption. If Regulation A is to have any issuer appeal and resurgence at all, the final rule that preempts tier 2 offerings from state registration must stand.

VII. FOR ARGUMENT'S SAKE

Although I hold firm to the conclusion that Congress should have let Regulation A lie and no attempt should have been made to revive it, the scholarly endeavor is incomplete if no effort is made to posit solutions to a suggested problem.[185] For argument's sake, if drafting the J.O.B.S. Act's Title IV were to be revisited or reconsidered, I would suggest the following:

184. *See FORM 1-A-Regulation A Offering Statement Under the Securities Act of 1933, pt. F/S, SEC*, https://www.sec.gov/about/forms/form1-a.pdf (form used in securities offerings made pursuant to Regulation A).

185. *See, e.g.*, Rutherford B. Campbell Jr., *Regulation A: Small Business' Search for a Moderate Capital*, 31 DEL. J. CORP. L. 77, 119-21 (2006) (discussing steps the commission should take to make Regulation A useful for small businesses).

A. *Title IV Should Explicitly Preempt All State Blue Sky Law Filing Requirements*

Instead of Congress placing the onus on the Commission to hold the line on state preemption, Congress in its drafting of the J.O.B.S. Act's Title IV should have explicitly exempted all Regulation A offerings from state registration and filing requirements. Its failure to do so is leading to predicted and foreseeable results – litigation. By not preempting all Regulation A filings explicitly through Title IV, state regulators see just enough legal uncertainty to make colorable claims that the Commission has overstepped its boundaries by creating a preemption that the Commission did not have the legal authority to create. That gap in Title IV's language has already sparked a trickle of lawsuits with the promise of more to follow.

In this environment of legal uncertainty, potential issuers will more than likely avoid the Regulation A exemption altogether. The last thing a small business needs in its early stages is potentially costly litigation.[186]

If Congress simply re-writes preemption into the Act itself then the whole interpretive fight that the Commission is currently facing goes by the way side. A simple act of Congress is all that is needed to side step this quagmire that will likely lead to ongoing and protracted litigation for the foreseeable future.

B. *The Fifty Million Dollar Cap Should be Lowered and the Annual Audited Financial Statement Requirement Should not be a Part of the Rule*

Each available offering exemption is a combination of tradeoffs between compliance costs to issuers and potential fraud exposure to investors. Generally speaking, the higher the exposure risk is to investors, the greater the compliance burden tends to be for the issuer.[187] When one offering exemption does a better job of balancing these two competing concerns, issuers tend to gravitate toward that exemption choice and will forego a more cumbersome option.

186. *See* Comment Letter from Rutherford B. Campbell, Jr. to Elizabeth M. Murphy, SEC Sec'y (Nov. 13, 2012), http://www.sec.gov/comments/jobs-title-iv/jobstitleiv-18.pdf (urging the Commission to preempt state securities laws in its rulemaking). The Commission ultimately wholesale adopted this very approach to preempt state securities laws in its rulemaking.

187. For example, Regulation D's Rule 504 caps the offering size at $1 million. 17 C.F.R. § 230.504(b)(2) (2015). In that instance, there are no investor qualifications nor is the issuer required to make any financial statement disclosures to its investors.

The problem with Regulation A is that it was out of balance at its inception with very high compliance hurdles where the corresponding benefit was capped at an offering size not to exceed five million dollars.[188] Though the J.O.B.S. Act has raised that cap to fifty million dollars for its Tier 2 offerings, it also raised the corresponding compliance hurdles causing Regulation A to continue to be out of balance between striking the right mix between investor protection and appropriate reasonable compliance requirements.

For Regulation A to have any possible appeal, the cost to meet its compliance requirements must be in step with the benefits that can be derived from choosing the exemption. The following then is suggested: to make Regulation A a more viable offering exemption, the exemption must accentuate those Regulation A aspects that make it unique from any other exemption. Accordingly, the exemption must be crafted to emphasize those unique Regulation A characteristics instead of blunting those characteristics, which is what has happened with this current Regulation A iteration under the J.O.B.S. Act and the Commission's final rulemaking.

Perhaps the two most unique Regulation A characteristics are the fact that Regulation A has no investor qualification requirements and that the issuer is allowed to advertise and solicit investors. As mentioned earlier, anyone can invest in a Regulation A offering regardless of net worth, income, or investor sophistication.[189] As to the second characteristic, the issuer is allowed to advertise and solicit investors and all of those solicited investors are eligible to participate in the offering.[190]

By contrast, newly revised Regulation D Rule 506(c) also allows the issuer to advertise and solicit investors, but the rule limits actual participation in the offering to accredited investors.[191] No other offering exemption allowed issuers the choice of publicly soliciting investors and keeping the pool of investors open to all regardless of financial sophistication or accredited investor status. Accordingly, it should follow that any Regulation A compliance or disclosure provisions should be crafted to allow the issuer to exploit and accentuate these two unique Regulation A offering characteristics. If Regulation A fails in this regard (which has been the case historically), then potential issuers will simply choose another exemption.

188. *See* 17 C.F.R. § 230.251(b) (2014) *amended by* 17 C.F.R. pt. 230 (2015) (specifying five million dollar limit).

189. *See generally* 17 C.F.R. § 230.251-.263 (2015) (revealing no investor qualifications or criteria in a review of Regulation A).

190. *Id*.

191. 17 C.F.R. § 230.506(c) (2015).

To take such advantage, first the Regulation A cap should be lowered. Fifty million dollars is too high and frankly is not necessary. If a company has grown to such a size that it is in a position to do a fifty million dollar offering, then the company is more likely suited for either a Rule 506 offering or perhaps even a public offering. Regulations A's Tier 2 offering regime as it is currently written is comparable to a public offering with no real discernible difference but for the fact that the Regulation A offering circular goes through a qualification process, whereas a full blown public offering would go through an SEC review process before being approved and declared effective. What then would be the reason for choosing Regulation A? What advantage would Regulation A provide that a full blown IPO would not? If we are being hyper technical, some would say that Regulation A allows the issuer to remain as a privately held company if that is the issuer's choice. But in reality would there be any discernible difference? If your offering is close to fifty million dollars, then it is more than likely you have a significant number of investors comprising your investor pool. A significantly large investor pool where each investor is investing a nominal amount is the only explanation. If the situation is any other, then Regulation A does not make sense where Rule 506 with no cap and no SEC qualification or SEC review process is involved. Accordingly, the fifty million dollar cap is too high and should be lowered.

The second suggestion would be to eliminate the audited financial statement requirement for Tier 2 offerings. Under the J.O.B.S. Act revisions for Tier 2 offerings, the issuer is required to include audited financial statements along with its Form 1-A Offering Statement.[192] Additionally, the issuer is required to file audited financial statements on an ongoing annual basis.[193] These audited financial statement requirements beg the question, "What is the audited financial statement's purpose?" Presumably, the purpose is to protect investors by providing them with financial statements that have been vetted by an independent third party. However, do audited financial statements make sense in the Regulation A context? As stated earlier, Regulation A's unique characteristics allow the issuer to publicly solicit investors and allow ANYONE regardless of their wealth, income, or financial savvy to participate in the offering. Assuming

192. Regulation A Offering Statement under the Securities Act of 1933, Form 1-A, 17 C.F.R. § 239.90 (2015) prescribes the informational filing and disclosure requirements for Regulation A offerings. 17 C.F.R. § 230.252(a) (2015). *See* 17 C.F.R. § 239.90 (requiring the use of Form 1-A for Regulation A offerings); S.E.C., Form 1-A — Regulation A Offering Statement Under the Securities Act of 1933, pt. F/S(c), https://www.sec.gov/about/forms/form1-a.pdf, *archived at* https://perma.cc/H6QP-GU3Q (requiring audited financial statements for Tier 2 Regulation A offerings).

193. *Id.*

this is the case, what then is the justification or necessity for audited financial statements? Audited financial statements would be prepared for an audience that likely has no interest in or is not otherwise inclined to read them.

One could argue that the audited financial statement requirement is there simply to act as an accountability check on the issuer. The assumption being that if they are required to prepare and file audited financial statements, then the likelihood that the issuer will act with integrity towards its investors increases: a valid argument. But the response hearkens back to the cost benefit assessment mentioned earlier. An effective Regulation A space should be one for smaller companies where the potential exposure to investors is limited by the company's size and the amount being invested by any one investor. In other words, if the parameters are set properly, then the protections are built in by the limited size and scope. Here, in its effort to revive Regulation A, Congress has stretched Regulation A beyond its intended borders. Accordingly, the cap should be lowered from $50 million to a size small enough such that removing the audited financial statement requirements can be justified. The exact number should be one that results from a study of the matter and an assessment as to where that "safe point" is realized. But $50 million is too high.

C. *Regulation A Should Have Only One Tier with All Filers Meeting the Same Requirements*

The Commission's final Regulation A rules should consist of one tier only with all filers having to meet the same requirements. As discussed earlier, the Commission's final Regulation A rules split the offering options into two tiers; Tier 1 and Tier 2.[194] Tier 1 is for offerings up to twenty million dollars and Tier 2 is for offerings between twenty million dollars and fifty million dollars.[195] The Tier 1 offering regime is exactly the same as the pre J.O.B.S. Act requirements with the exception being that the limit is raised from five million dollars to twenty million dollars.[196] Also, Tier 2, as discussed earlier, allows for offerings between twenty million dollars and fifty million dollars but with rigorous disclosure requirements which

194. 17 C.F.R. § 230.251(a) (2015).

195. *Id.*

196. *Compare* 17 C.F.R. §§ 230.251(a)(1), .252, .257 (2015) *with* 17 C.F.R. § 230.251, .252, .257 (effective to June 18, 2015) (showing that Tier 1 offerings only differ from the previous, single-tier offering regime in aggregate amount of capital raised).

include annual reporting and audited financial statements.[197]

The Commission's final rulemaking with Regulation A's two tiered regime highlights the fundamental problem with Congress's attempt to re-work Regulation A to begin with. The whole rule making endeavor was done devoid of any focus or consideration for those that would be potential Regulation A users. Regulation A's intended audience was to be SMALL businesses; small meaning total assets more in the $50,000 - $5 million range.[198] Again, this is based on a review of the forty-two Regulation A filings that were sampled for this article. Based on these numbers and based on the Regulation A requirements, it is foreseeable that most of the potential Regulation A filers would be in that Tier 1 category, the category whose requirements are exactly the same as the pre J.O.B.S. Act version. These are the same requirements that caused issuers to avoid Regulation A in the first place.

The turf war between the state and federal regulators over this topic has caused both sides to engage in a legislative and rule making process resulting in no meaningful improvements to Regulation A whatsoever. The same issuers that avoided Regulation A prior to the J.O.B.S. Act will continue to avoid it under the Commission's revised rules because the same onerous requirements remain. Any issuer who is in a position to offer securities for more than twenty million dollars would have virtually no reason to use Regulation A as there are other exemptions that work much better for larger offerings.

The end result after the J.O.B.S. Act and the Commission's subsequent rulemaking for Regulation A, is virtually no change as the large majority of potential Regulation A filers would more than likely fall into the Tier 1 category. This tier has the same disincentivizing provisions that existed prior to the J.O.B.S. Act.

In sum, the suggestions are 1) re-write the J.O.B.S. Act provision and explicitly allow for all state blue sky law preemption; 2) lower the $50 million cap to a level better suited for Regulation A and its intended audience; 3) remove both the audited financial statement filing requirement and the ongoing annual audited financial statement disclosure requirement; and 4) have only one tier with all Regulation A filers meeting the same requirements.

I continue to hold firm to the position that Regulation A was a flawed exemption at inception and the proposed revisions will not change those

197. 17 C.F.R. §§ 230.251(a)(2), .257(b) (2015).

198. *See* Jumpstart Our Business Startups Act (J.O.B.S. Act), Pub. L. No. 112-106, 126 Stat. 306, tit. IV (codified as amended in scattered sections of 15 U.S.C.) ("Small Company Capital Formation").

flaws. But, if Regulation A has *any* chance of succeeding, then state preemption must be a part of the new rule and audited financial statements in any capacity must be excluded. Again this is simply a matter of tailoring the exemption's contours with the exemption itself. For whom was Regulation A intended? What type of issuer and what type of investor? From looking at the Rule's language, the intended investor was presumably a small to mid-size company with assets in the zero to $5 million range. As far as the investors are concerned, Regulation A was drafted to allow for investors with little net worth, who earn modest incomes, and who have little, if any, financial sophistication. Assuming that these are the types of investors that the exemption contemplates, what is the need for audited financial statements? For whom are these statements being prepared? Likewise, what is the rationale for an offering size as high as $50 million? Again, if a company has grown to the point where it is in a position to do a $50 million offering, then it has out grown anything that Regulation A would have to offer. This is a company that, at the very least, would either be looking to do an offering under Rule 506 if not a full-blown public offering.

Congress should have given more thought to its targeted investor. The J.O.B.S. Act's current Regulation A revisions appear to have been done so without regard for both its targeted issuers and targeted investors. Perhaps a re-working with these two constituents in mind would lead to a better and more thoughtful result. I still hold firm that Regulation A should be done away with altogether. But if Regulation A is to have any chance at revival, then some of those aspects should be revisited.

VIII. CONCLUSION

Regulation A was a flawed private offering exemption at its inception. The offering exemption was intended to be available to issuers who wished to include investors with modest income, modest net worth, and little, if any, financial sophistication. But the problem with this targeted directive is that investors in this demographic are generally too scarce to serve as a viable demographic for most private offerings and likewise are too problematic to be worth the trouble of courting.

Accordingly, the meager benefits for choosing the Regulation A route are disproportionate compared to the cost involved in terms of both time and money to comply. The modifications under the J.O.B.S. Act will do little, if any, to rectify this imbalance. Regulation A was never intended to be an exempt offering that allows for the raising of up to fifty million dollars; especially where there are other exempt offering alternatives that are much better suited for offerings of this size. The added compliance burdens of audited financial statements required both at filing and on an annual basis again are compliance mandates that show Congress' lack of regard for its targeted audience. Finally, even without all the problems mentioned above, the whole state preemption debacle alone is enough to cause issuers to tack away from Regulation A's potential quagmires. The fight between the state regulators and the Commission over this issue is a classic case of a political war being fought with no regard for practical realities. If the state regulators ultimately win this fight, they will have won a battle that will assure them losing the war as a state filing requirement will almost assure Regulation A's continued dormancy and eventual extinction. Regulation A was a flawed offering exemption at its inception. Sometimes the most appropriate thing to do is to let sleeping regulations lie.

APPENDIX: PART A

NOTE: 42 Regulation A filings were reviewed. Specific information was gathered and summarized in Part B of this Appendix.

Company Name	Filing Date
1. EQUITYPOINT, LLC	**FILING DATE:** 12-2008
2. OAKLEYS SHOOTING RANGE, INC.	**FILING DATE:** 2-2009
3. LYONS BANCORP, INC.	**FILING DATE:** 2-23-2004
4. THE GODSPELL LLC	**FILING DATE:** 2-23-2010
5. RESONANT SOFWARE, INC.	**FILING DATE:** 2-2009
6. RICHLAND RESOURCES CORP.	**FILING DATE:** 8-2010
7. FREE MOVERS, INC.	**FILING DATE:** 7-2010
8. ABL FILM AND ENTERTAINMENT CORP.	**FILING DATE:** 3-2010
9. RECOVERY ENTERPRISES, INC.	**FILING DATE:** 7-31-2009
10. REAL SPORTS INVESTMENTS, LLC	**FILING DATE:** 2-26-2008
11. ACTIONVIEW INTERNATIONAL, INC.	**FILING DATE:** 3-10-2010
12. MNB TECHNOLOGIES, INC.	**FILING DATE:** 8-17-2011
13. LONE MOUNTAIN MINING COMPANY	**FILING DATE:** 3-25-2009
14. JUMPSTART MARKETING, INC.	**FILING DATE:** 12-18-2008
15. LIGHTSPEED SYSTEMS, INC.	**FILING DATE:** 6-2008
16. EARTHMETRIX TECHNOLOGIES, INC.	**FILING DATE:** 2-2008
17. EMERGING GROWTH FUNDING, INC.	**FILING DATE:** 6-2009
18. FREEDOM MOTORS, INC.	**FILING DATE:** 5-2011

19. CARDIOMEDICS, INC.	**FILING DATE:** 2-2009
20. ENERGY CONSERVATION TECHNOLOGIES, INC.	**FILING DATE:** 11-2008
21. EL CHUPACABRA, INC.	**FILING DATE:** 5-19-2010
22. THE CARLYLE ULTRA, INC.	**FILING DATE:** 11-2010
23. EQUITYPOINT, LLC FUND I SERIES	**FILING DATE:** 8-2008
24. HOME DECORATION, INC.	**FILING DATE:** 8-2009
25. GILPIN COMPUTER CONSULTANTS, INC.	**FILING DATE:** 2-2009
26. BANK OF IDAHO HOLDING CO.	**FILING DATE:** 6-2010
27. AFRO DOLLAR INC.	**FILING DATE:** 10-17-2011
28. ACTIVE CARE AT BRESSI RANCH LLC.	**FILING DATE:** 7-13-2011
29. BIDDEFORD AND SACO WATER CO.	**FILING DATE:** 5-28-2010
30. AGRI-LABORATORIES, LTD.	**FILING DATE:** 6-17-2008
31. ENTERTAINMENT ARTS RESEARCH, INC.	**FILING DATE:** 4-28-2010
32. ENVIRO-SERV, INC.	**FILING DATE:** 5-20-2014
33. METATRON, INC.	**FILING DATE:** 5-1-2014
34. NETWORKED EMERGENCY SYSTEMS, INC.	**FILING DATE:** 5-6-2014
35. MANEGAIN, INC.	**FILING DATE:** 5-6-2014
36. CYBER HOLDINGS, INC.	**FILING DATE:** 5-3-2014
37. EASTON PHARMACEUTICALS INC.	**FILING DATE:** 5-15-2014
38. CREDITSMARTPRO, INC.	**FILING DATE:** 5-7-2014
39. COMMONWEALTH NEW ERA RACING, LLC.	**FILING DATE:** 5-6-2014

40. CODE NAVY	**FILING DATE:** 4-17-2014
41. BIOSCULPTURE TECHNOLOGY, INC.	**FILING DATE:** 5-8-2014
42. ALAMO PARTNERS, LLC	**FILING DATE:** 3-14-2014

APPENDIX: PART B

NOTE: Part B is a summary of information gathered on seven specific categories. These categories were used to assess the type of investor the filer was seeking to participate in its offering.

INVESTOR CRITERIA/ CATEGORY	COMPANY NUMBER AND NAME
1. **Issuer limits offering to accredited Investors only**	**1. EQUITYPOINT, LLC** (See Exhibit C – Subscription Agreement- Section B, pg. 99 – "Investor Qualification" – Investor required to attest to accredited investor criteria such as individual income greater than $200,000 or net worth greater than $1,000,000) **6. RICHLAND RESOURCES CORP.** (Shares being offered exclusively to Texas residents who are accredited investors. Offering Statement, pg. 4) **23. EQUITYPOINT, LLC FUND I SERIES** (See Exhibit C – Subscription Agreement- Section B, pg. 99 – "Investor Qualification" – Investor required to attest to accredited investor criteria such as individual income greater than $200,000 or net worth greater than $1,000,000) **32. ENVIRO-SERV, INC.** (Offering made primarily to one large investor committed to purchasing $1,000,000 of the $1,500,000 worth of shares being offered. (pg. 12). The investor attested to being an accredited investor as set forth in the Investment Agreement § 3.4, pg. 67) **33. METRATON, INC.** (Offering made primarily to one large investor committed to purchasing all of the $1,500,000 worth of shares being offered. (pg. 11). The investor

	attested to being an accredited investor as set forth in the Investment Agreement § 3.4, pg. 94) 37. **EASTON PHARMACEUTICALS INC.** (Offering made primarily to one large investor committed to purchasing up to $5,000,000 of the $5,000,000 worth of shares being offered. (pg. 13). The investor attested to being an accredited investor as set forth in the Investment Agreement § 3.4, pg. 114)
2. **Issuer limits offering to "Sophisticated Investors"**	9. **RECOVERY ENTERPRISE, INC.** (Investor must attest to being knowledgeable and experienced in finance, securities, and investments. See Exhibit 4- Subscription Agreement section 2.1(C) – pg. 74) 11. **ACTIONVIEW INTERNATIONAL, INC.** (Investor must attest to being knowledgeable and experienced in finance and business matters. See Exhibit 4.1 – Subscription Agreement – § 3.3) 15. **LIGHTSPEED SYSTEMS, INC.** (See Exhibit 4 - Subscription Agreement, Section 4(c) – pg. 119 – Investor attesting to having knowledge and experience in financial and business matters) 38. **ENERGY CONSERVATION TECHNOLOGIES, INC.** (See Subscription Agreement, Section 4(c) – pg. 52 – Investor attesting to having knowledge and experience in financial and business matters)
3. **Issuer limits offering to investors who have a net worth of**	4. **THE GODSPELL, LLC** (Investor must have a minimum net worth of $60,000 (exclusive of house, furniture, and automobiles) and must

at least $225,000 and an income of at least $60,000	have an annual gross income of at least $60,000. Alternatively, the investor must have a liquid net worth of at least $225,000. See Offering Circular Summary, pg. 11) 28. **ACTIVE CARE AT BRESSI RANCH LLC.** (Net worth greater than $250,000 or income greater than $70,000 and a net worth of at least $70,000. See Offering Statement, pg. 3 "Who May Invest" section)
4. **Minimum investment of $1,000 or more**	1. **EQUITYPOINT, LLC** (minimum investment of $2,500 – Exhibit C – Subscription Agreement – Section A – pg. 94) 4. **THE GODSPELL, LLC** (minimum investment of $1,000. Part II-Offering Circular, pg. 5) 9. **RECOVERY ENTERPRISES, INC.** (minimum investment of $1,200. Part II Offering Circular, pg. 8) 20. **ENERGY CONSERVATION TECHNOLOGIES, INC.** (Minimum investment of $11,000. See Part II "Preliminary" Offering Circular, pg. 7) 23. **EQUITYPOINT, LLC FUND I SERIES** (minimum investment of $2,500 – Exhibit C – Subscription Agreement – Section A – pg. 93) 26. **BANK OF IDAHO HOLDING CO.** (minimum investment for new shareholders is $249,750. See Offering Statement, pg. 12, first page of Preliminary Offering Circular) 27. **AFRO DOLLAR INC.** (minimum investment of $1,000. See Offering Statement, pg. 8)

	28. ACTIVE CARE AT BRESSI RANCH LLC. (minimum purchase requirement of 20 units at $1,000 per unit ($20,000). See Offering Statement – Preliminary Offering Circular, pg. 1) **29. BIDDEFORD AND SACO WATER CO.** (minimum investment is 1 unit for $10,000 per unit. See Offering Statement – Part II – Offering Circular – pg. 4) **42. ALAMO PARTNERS, LLC** (minimum investment amount of $10,000 per subscriber. See Offering Circular, pg. 19)
5. **Offerings prepared without counsel's assistance**	**7. FREE MOVERS, INC.** (offering statement handwritten; space left blank as to issuer's counsel. See Offering Statement, Part I, Item 1(h), pg. 2) **10. REAL SPORTS INVESTMENT LLC** (offering statement handwritten; no issuer's counsel listed. See Offering Statement, Part I, Item 1(h), pg. 2) **11. ACTION VIEW INTERNATIONAL, INC.** (offering notes specifically that counsel was not engaged to draft offering statement. See Offering Statement – Part I - Item 1 Significant parties – pg. 2) **12. MNB TECHNOLOGIES, INC.** ("none" noted for issuer's counsel. See Offering Statement, Part I, Item 1(h), pg. 2) **17. EMERGING GROWTH FUNDING, INC.** (issuer's counsel not listed. See Offering Statement, Part I, Item 1(h), pg. 3) **22. THE CARLYLE ULTRA, INC.** (issuer's counsel listed as "n/a." See Offering

	Statement, Part I, Item 1(h), pg. 3) 24. **HOME DECORATION, INC.** (offering statement handwritten; issuer's counsel listed as "n/a." See Offering Statement, Part I, Item 1(h), pg. 2) 25. **GILPIN COMPUTER CONSULTANTS, INC.** (issuer's counsel listed as "none." See Offering Statement, Part I, Item 1(h), pg. 2) 27. **AFRO DOLLAR INC.** (offering statement handwritten; "none" listed next to issuer's counsel. See Offering Statement, Part I, Item 1(h), pg. 3) 42. **ALAMO PARTNERS, LLC** ("none" noted under issuer's counsel. See Offering Statement, Part I, Item 1(c), pg. 2)
6. **Clear intention of doing public solicitation**	1. **EQUITYPOINT, LLC** (See "Plan of Distribution," pg. 23 – Plan to offer 200,000 preferred units to the public) 4. **THE GODSPELL LLC** (securities being offered to residents of New York, California, Connecticut, Illinois, Louisiana, Massachusetts, Michigan. Managing members will be offering securities through solicitation, word of mouth, and the internet. See Offering Statement, Part I, Item 4, pg. 3) 19. **CARDIOMEDICS, INC.** (company states explicitly that it is offering its shares to the public at a price of $1.00 per share. See "The Offering & Plan of Distribution. Offering Statement, Part I, pg. 13) 21. **EL CHUPACABRA, INC.** (shares being offered through Internet to residents of California, New York, and Pennsylvania. See Offering Statement, Part I, ITEM 4, pg. ii)

	22. **THE CARLYLE ULTRA, INC.** (securities being sold through nationally registered and sanctioned brokerages and may eventually be listed through other public mediums. See Offering Statement, Part I, ITEM 4, pp. 3-4) 23. **EQUITYPOINT, LLC FUND I SERIES** (securities being offered to residents of Indiana, Illinois, Kentucky, Massachusetts, Delaware. Managers plan on advertising using billboard, radio and television, advertisements, and newspapers. Offering Statement, Part I Item 4 – pg. 2) 25. **GILPIN COMPUTER CONSULTANTS, INC.** (shares being offered to all 50 U.S. states. See Offering Statement, Part I – Item 4, pg. 2) 27. **AFRO DOLLAR INC.** (shares being offered to residents of Illinois, Alabama, California, Florida, Georgia, Louisiana, Maryland, Michigan, Minnesota, Mississippi, Missouri, New Jersey, New York, North Carolina, Ohio, Pennsylvania, South Carolina, Texas, Virginia, Wisconsin, Washington D.C. See Part II – Offering Circular, pg. 13) 31. **ENTERTAIMENT ARTS RESEARCH INC.** (Distribution plan includes sales on public markets and exchanges. pg. 25)
7. **Filings that were actively seeking investors regardless of income, net worth, or financial sophistication**	10. **REAL SPORTS INVESTMENT LLC** (Company specifically targeting sports fans due to the fact they (sports fans) will have the most knowledge and interest in a security encompassing RSI's business model. See Offering Statement, Part II Offering Circular, "BUSINESS AND PROPERTIES" section)

	18. FREEDOM MOTORS, INC. (Company has no minimum investment amount and its shares were being offered at $2.50 per share. See "Plan of Distribution" section in Part II – Offering Circular, pg. 13) **19. CARDIOMEDICS, INC.** (Shares being offered for $1.00 per share with no minimum investment amount. See Offering Statement, pg. 13)