

Heads Up

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The primary objective of the Act is to “increase American job creation and economic growth by improving access to the public capital markets for emerging growth companies.”

IPO On-Ramp

JOBS Act to Ease Access to Investment Capital

by Joe DiLeo and Ken Pressler, Deloitte & Touche LLP

Introduction

On April 5, 2012, President Obama signed the JOBS Act¹ into law. The primary objective of the Act is to “increase American job creation and economic growth by improving access to the public capital markets for emerging growth companies.”

Editor’s Note: Response to the JOBS Act has been mixed. Although it has received very strong support on Capitol Hill, many have expressed concern that several of the changes resulting from the Act could erode investor protections and eliminate disincentives to engaging in fraudulent practices.

To help reduce the burden smaller companies face in obtaining capital, the JOBS Act limits some of the regulatory requirements introduced by the Sarbanes-Oxley Act of 2002 by, for example:

- Creating an exemption for “crowdfunding” transactions.
- Increasing shareholder thresholds that trigger public company registration and reporting requirements under the Securities Exchange Act of 1934 (the “Exchange Act”) from 500 shareholders of record to 2,000 shareholders of record.

Perhaps the most notable change, however, is the creation of the “emerging growth company” (EGC), a new type of issuer whose less stringent regulatory and reporting requirements are intended to encourage public offerings by small and developing companies. Provisions of the JOBS Act that apply to EGCs include the following:

- Only two years of audited financial statements are required in an initial public offering (IPO) and other registration statements.
- The periods required for selected financial data in both registration statements and periodic filings do not extend to periods before the first year presented in the EGC’s IPO.
- An EGC is exempt from the requirement to obtain an attestation report on internal control over financial reporting (ICFR) from its auditor.
- An EGC does not need to adopt new accounting standards until they become effective for private companies (i.e., nonissuers).

Emerging Growth Companies

Title I of the JOBS Act outlines the requirements for EGC status under the SEC’s reporting

¹ The Jumpstart Our Business Startups Act.

Under the Act, for a company to be considered an EGC, its total gross revenues cannot exceed \$1 billion in its most recently completed fiscal year.

framework. Under the Act, for a company to be considered an EGC, its total gross revenues cannot exceed \$1 billion in its most recently completed fiscal year. EGC status can be held for up to a maximum of five years after an IPO as long as (1) the EGC's total gross revenues do not exceed \$1 billion during the five-year period, (2) the EGC's market capitalization does not exceed \$700 million (i.e., the EGC does not meet the definition of a large accelerated filer), or (3) the EGC does not issue more than \$1 billion in nonconvertible debt in a three-year period. A company that completed an IPO on or before December 8, 2011, is not eligible for EGC classification.

Editor's Note: On April 16, 2012, the SEC's Division of Corporation Finance published its first batch of [frequently asked questions](#) (FAQs) on Title I of the JOBS Act (see the appendix of this *Heads Up* for additional information). In [FAQ 2](#), the SEC staff noted that the JOBS Act effective date for an EGC is the initial sale of common equity securities (whether for cash or to employees on Form S-8) occurring on or after December 8, 2011, "[e]ven if the issuer had a registration statement declared effective on or before December 8, 2011, so long as the first sale of common equity securities occurs after [such date]."

Reduced Financial Information

Section 102 of the JOBS Act amends the Securities Act of 1933 (the "Securities Act") and the Exchange Act to lessen SEC reporting requirements for companies that qualify as EGCs. In registration statements (IPO and other) and periodic filings, EGCs are required to present only two years of audited financial statements. The Act also limits the periods required to be presented within selected financial data² in an EGC's registration statements and periodic filings to the earliest year that audited financial statements were presented in the EGC's IPO registration statement. See [FAQs 11 and 12](#) for additional guidance on applying these provisions.

Accounting Standards

An EGC also benefits from a provision in Section 102 of the JOBS Act that allows it to adopt new or revised financial accounting standards on the basis of effective dates applicable to private companies (i.e., nonissuers) "if such standards apply to companies that are not issuers."

Editor's Note: In [FAQs 33 and 35](#) (in the SEC's second batch of FAQs on Title I of the JOBS Act), the staff (1) confirmed that only new and revised accounting standards may be deferred and (2) clarified that the term "new or revised" means "any update **issued** by the Financial Accounting Standards Board to its Accounting Standards Codification after April 5, 2012, the date of the enactment of the JOBS Act" (emphasis added). See the [appendix](#) of this *Heads Up* for a summary of additional interpretive guidance on the JOBS Act.

Auditor-Related Changes

The JOBS Act amends Section 404(b) of the Sarbanes-Oxley Act by exempting EGCs from the requirement to obtain an attestation report on the company's ICFR from its registered public accounting firm. EGCs are exempted from any future PCAOB rules that may require auditor rotation or potential rules calling for the expansion of the auditor's report to include an auditor's discussion and analysis of the company under audit. In addition, other PCAOB rules that are adopted after the passage of the JOBS Act would apply to EGCs only if the SEC determined that the rules were designed to promote investor protection and that applying such rules to EGCs would be in the best interest of the investing public. These changes would apply to EGCs as long as they remained EGCs.

Confidential Reviews of Draft IPO Filing Materials

Title I of the JOBS Act changes the Securities Act to allow an EGC to provide a confidential draft IPO registration statement to the SEC staff for review before its public filing (i.e., the SEC is prohibited from disclosing the information being reviewed).

² As required in SEC Regulation S-K, Item 301, "Selected Financial Data."

The JOBS Act relaxes certain restrictions on communications among investors, brokers, and analysts involved in an IPO.

However, an EGC is required to publicly file such draft and any related amendments with the SEC no later than 21 days before its “road show.”³

Increased Flow of Information

The JOBS Act relaxes certain restrictions on communications among investors, brokers, and analysts involved in an IPO. The Securities Act is amended to allow oral or written communications that gauge investor interest in a potential offering before or after the filing of a registration statement (commonly referred to as “testing the waters”). Such communications could be made by the EGC or a person authorized to act on its behalf; however, they could only be made to investors that are qualified institutional buyers or accredited investors.⁴

The JOBS Act also amends the Securities Act to allow brokers, dealers, or members of a national securities exchange to more freely distribute or publish research reports about an EGC and prohibits the SEC or national securities associations from creating rules that would restrict such flow of information among the parties to an EGC’s IPO transaction. Conforming changes must also be made to the Exchange Act to prohibit the SEC or any national securities exchange from restricting or limiting (1) the parties that could arrange and participate in communications between securities analysts and any potential investors (i.e., brokers, dealers, and national securities association members) and (2) the distribution of research reports or the making public of appearances regarding the securities being offered.

Executive Compensation

Under the JOBS Act, EGCs can meet the SEC’s executive compensation reporting requirements by providing the same reduced disclosures that are required of smaller reporting companies under Rule 12b-2 of the Exchange Act. The JOBS Act also amends certain provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act to exclude EGCs from their requirements. These amendments include:

- An exemption that precludes EGCs from calculating and disclosing the ratio of the CEO’s compensation to the median compensation of all other employees.
- An exemption from the “say-on-pay,” “say-on-frequency,” and “say-on-golden parachute” requirements; however, under Section 102 of the JOBS Act, once an issuer loses EGC status, it would need to comply with the executive compensation advisory votes one year after losing such status (or three years if the issuer was an EGC for less than two years from its IPO date).

Other Changes Related to EGCs

Issuers that qualify as EGCs under the JOBS Act are not required to become EGCs. If such issuers choose to forego EGC status, they are subject to all the requirements of non-EGCs (i.e., they may not apply a hybrid approach). Title I of the JOBS Act also directs the SEC to examine Regulation S-K to determine ways to modernize and further streamline reporting processes for EGCs.

Editor’s Note: In [FAQ 7](#), the SEC staff confirmed that except for “accounting standards referenced in . . . Section 107(b) of the JOBS Act . . . an [EGC] may decide to follow only some of the scaled disclosure provisions.”

Crowdfunding Exemption

The JOBS Act directs the SEC to create an exemption from Securities Act registration requirements for “crowdfunding” transactions meeting certain criteria. Crowdfunding allows a company to gain access (through social media or other means) to a large pool of investors that contribute small amounts as a means to raise capital and achieve growth. Securities purchased by investors through crowdfunding transactions are not considered “held of record” and thus are excluded from an issuer’s shareholder cap.

³ An investor “road show” typically consists of presentations to analysts, fund managers, and other potential investors to promote a company’s securities’ offering and to assess interest in the securities being offered.

⁴ As such terms are defined in Rules 144A and 501(a) of the Securities Act.

The JOBS Act directs the SEC to create an exemption from Securities Act registration requirements for “crowdfunding” transactions meeting certain criteria.

To qualify for the exemption, the offering intermediary (e.g., a broker-dealer or funding portal) cannot offer investment advice, solicit the details of the offering, or advertise the sale of securities. The exemption allows the issuer to annually offer up to \$1 million of securities. Investor safeguard provisions limit the amount of the funds that may be contributed by an individual investor on the basis of annual net income or net worth.

An issuer of securities in a crowdfunding transaction is also be required to file certain information with the SEC and to give the intermediary and investor group specific information about the issuer and the transaction. The intermediary acting as the broker or funding portal is required to register with the SEC and any self-regulatory organization (if applicable) and would be required, among other things, to take certain actions specifically designed to:

- Reduce the risk of fraud.
- Sufficiently inform investors of the investment risks, including those related to an investor’s restriction from transferring its ownership interests for one year.
- Provide for civil liability protection from misstatements or material omissions in the offering materials.
- Ensure that investors included in the pooled transaction do not exceed the investment limits in the aggregate if participating in multiple offerings in a given year.

Small Company Capital Formation

Title IV of the JOBS Act increases the limit on filings of exempt offerings currently subject to Regulation A of the Securities Act from \$5 million annually to \$50 million annually and adds a civil liability provision related to the offering or sale of securities. The JOBS Act also requires the issuer to (1) file annual audited financial statements with the SEC, (2) make certain periodic nonfinancial disclosures to investors, and (3) file and distribute an offering statement to prospective investors. In addition, the SEC is required every two years to revisit (and potentially increase) the limits on exempt securities offerings and, if no changes are made, report to Congress its reasons for not increasing the limits.

Shareholder Thresholds for Reporting

Under the JOBS Act, Section 12(g) of the Exchange Act is amended to increase the shareholder threshold that triggers the requirement for companies to register with the SEC from 500 to 2,000 shareholders of record. For private companies that are not banks or bank holding companies, no more than 499 shareholders of record may be nonaccredited investors. In addition, like securities offered in a crowdfunding transaction, securities offered to employees under an employee compensation arrangement are excluded in the determination of the number of shareholders of record.

Access to Capital in Private Offerings

To eliminate the ban on general solicitation and advertising for private offerings, Title II of the JOBS Act directs the SEC to amend Rule 506 of Regulation D and Rule 144A of the Securities Act within 90 days of its enactment. However, the Act limits the general solicitation and advertising to (1) accredited institutional investors in Rule 506 offerings and (2) qualified institutional buyers in offerings under Rule 144A. The Securities Act is also amended to exempt any person selling securities in a Rule 506 offering from broker-dealer registration requirements as long as certain conditions are met regarding compensation and management of the funds exchanged in the offering.

Appendix — Implementation Guidance and Announcements Related to the JOBS Act

The paragraphs below discuss certain announcements and implementation guidance issued by the SEC shortly after the JOBS Act's passage.

May 3, 2012 — Additional Title I FAQs Issued

The SEC staff published its second batch of [FAQs](#) on Title I of the JOBS Act. Many of the FAQs address implementation of the Act's provisions by EGCs. Topics include (1) determining whether an issuer qualifies for EGC status; (2) understanding how certain provisions of the Act interact with existing SEC rules and regulations related to smaller reporting companies, asset-backed securities issuers, and foreign private issuers; and (3) applying certain of the financial reporting and disclosure accommodations available to EGCs (e.g., deferral of the adoption of new and revised accounting standards).

Extended Transition Provisions Related to Adoption of Financial Accounting Standards

- The SEC staff confirmed that only "new or revised" accounting standards may be deferred. It also clarified that the term "new or revised" means "any update issued by the Financial Accounting Standards Board to its Accounting Standards Codification after April 5, 2012, the date of the enactment of the JOBS Act." See FAQs 33 and 35.
- The staff clarified that after initially electing to take advantage of the extended transition provisions to adopt financial accounting standards, an EGC may later elect to adopt accounting standards with effective dates applicable to non-EGCs. The staff will not object to this "opt-in" election, which is irrevocable, provided the issuer complies with Sections 107(b)(2) and (b)(3) of the JOBS Act and the election is prominently disclosed in the next registration statement or periodic filing after the election is made. See FAQ 37.

Confidential SEC Staff Review of IPO Registration Statements

- The SEC staff noted that if, in a submission for a confidential review, an EGC includes financial statements that have been restated to correct a material error, the EGC's financial statements should contain the appropriate restatement disclosures required by ASC 250-10-50¹ until its financial statements are updated for the next annual period. See FAQ 38.
- The staff confirmed that no earlier than 20 days after a registration statement is effective it will make available publicly on EDGAR (1) comment letters resulting from its confidential reviews of an EGC's registration statement and (2) the EGC's responses to the comment letters. In addition, the SEC staff clarified that EGCs seeking confidential treatment for any portion of a response to an SEC staff comment letter would need to indicate that explicitly and follow [Rule 83 procedures](#). See FAQs 25 and 26.

Editor's Note: Issuers are encouraged to consult with their legal counsel before filing a confidential treatment request to determine whether their requests meet the requirements of Rule 83 and [Staff Legal Bulletin No. 1](#). Because an EGC would be required to post its comment letter responses on EDGAR, issuers are encouraged to complete such consultations before responding to an SEC comment letter received during a confidential review.

Foreign Private Issuers

- The SEC staff indicated that "notwithstanding Section 7(a)(2)(A) of the Securities Act," a foreign private issuer (FPI) that qualifies for EGC status and is either a first-time IFRSs adopter or retrospectively applies an IFRS accounting policy must file three statements of financial position in its IPO registration statement to support its assertion (under IFRS 1) that it complies with "IFRS as issued by the IASB." See FAQ 39.
- The staff clarified that an FPI qualifying for EGC status and reconciling its home country GAAP to U.S. GAAP may elect to use the extended transition period for new or revised financial accounting standards in its U.S. GAAP reconciliation. See FAQs 34 and 36.

April 23, 2012 — Staff Makes Announcement About Crowdfunding Exemption

The SEC staff [reminded](#) issuers that the JOBS Act requires the SEC to promulgate rules to implement an exemption that allows "crowdfunding." The staff warned that until such rules are adopted, transactions that rely on the exemption are unlawful.

¹ For titles of FASB Accounting Standards Codification (ASC) references, see Deloitte's ["Titles of Topics and Subtopics in the FASB Accounting Standards Codification."](#)

April 16, 2012 — FAQs Issued on General Applicability of Title I

The SEC staff published 17 [FAQs](#) on the general applicability of Title I of the JOBS Act. Among other topics, the FAQs provide general implementation guidance on determining how and when an issuer evaluates whether it qualifies for EGC status. For example, the SEC staff:

- Confirmed that except for “accounting standards referenced in . . . Section 107(b) of the JOBS Act . . . an [EGC] may decide to follow only some of the scaled disclosure provisions.” See FAQ 7.
- Noted that an EGC would evaluate whether it may submit a registration statement or related amendment for confidential review at the time of submission. See FAQ 3.
- Clarified that the initial filing date is not synonymous with the date a draft is submitted for confidential review. For example, the initial filing date is the date the IPO registration statement is filed publicly. For confidential submissions, such date must be at least 21 days before a “road show.” See FAQs 3 and 13.
- Indicated that the form and content requirements for the IPO registration statement are evaluated when it is initially filed. See FAQ 3.
- Discussed situations in which EGC status is lost during the registration statement process. See FAQ 3.
- Addressed how, in determining whether EGC status is initially met and retained, an issuer would calculate (1) annual gross revenues and (2) nonconvertible debt issued during the previous three-year period. See FAQs 1 and 17.
- Noted how certain JOBS Act provisions for scaled disclosures interact with other rules under SEC Regulations S-X and S-K (e.g., other entities’ financial statements required under Regulation S-X, Rules 3-05 and 3-09, and certifications under Section 906 of the Sarbanes-Oxley Act). See FAQs 15 and 16.
- Confirmed that the JOBS Act effective date for an EGC is the initial sale of common equity securities (whether for cash or to employees on Form S-8) occurring on or after December 8, 2011, “[e]ven if the issuer had a registration statement declared effective on or before December 8, 2011, so long as the first sale of common equity securities occurs after [such date].” See FAQ 2.

April 11, 2012 — FAQs Issued on Changes to Requirements for Exchange Act Registration and Deregistration

The SEC staff published an [FAQ document](#) containing the staff’s interpretive guidance on issuers’ registration and deregistration thresholds under Sections 12(g) and 15(d) of the Exchange Act, including questions about determining “holders of record” for such thresholds.

April 10, 2012 — FAQs Issued on Confidential Submission Process for EGCs

The SEC staff published [FAQs](#) containing the staff’s interpretive guidance on matters related to the confidential review process that applies to EGCs under the JOBS Act. Among other topics, the FAQs confirm that (1) Exchange Act registration statements (e.g., Forms 10 and 20-F) are not eligible for confidential review, (2) confidentiality requests (under Rule 83) are not required for such submissions, and (3) the Securities Act Rule 134 safe harbor “is not available until [an] issuer files a registration statement that satisfies the requirements of Rule 134” (i.e., a company may not rely on the Rule 134 safe harbor for public communications made after a confidential submission). In addition, the FAQs address various questions about how an EGC should determine when it must make registration statements publicly available (that were reviewed confidentially).

April 5, 2012 — Announcement Made Regarding Confidential Review Process for EGCs

The SEC staff [announced](#) that it has discussed the process by which an EGC would temporarily submit a registration statement for confidential review until the EDGAR system is equipped to receive electronically uploaded documents. Domestic and foreign EGCs are requested to “submit draft registration statements in a text searchable PDF file on a CD/DVD” or “in paper” and should include a transmittal letter confirming EGC status. In addition, non-EGC foreign private issuers that are eligible for confidential reviews (i.e., under an existing SEC staff policy) are now required to follow the same process as the one described for EGCs.

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