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A Whirlwind Recap of the SEC's Principal 2020 Rulemakings

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Agenda

- Financial Disclosures About Guarantors and Issuers of Guaranteed Securities
- Securities Offering Reform for BDCs and Closed-End Funds
- Amendments to Financial Disclosures about Acquired Businesses
- Amending the “Accredited Investor” Definition
- Amendments to the Exempt Offering Framework
- Modernization of Regulation S-K Items 101, 103 and 105
- Amendments to MD&A
- Modernization of Shareholder Proposal Rules/14a-8

Amendments to Financial Disclosures About Guarantors and Issuers of Guaranteed Securities

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Financial disclosures about guarantors and issuers of guaranteed securities

- On March 2, 2020, the SEC amended financial disclosure rules in registered debt offerings involving guaranteed or collateralized securities under Rules 3-10 and 3-16 of Regulation S-X
- Aims to improve quality of disclosure, encourage issuers to conduct debt offerings on a registered basis and reduce compliance costs
- **Effective Date**: January 4, 2021
- Amendments revise Rules 3-10 and 3-16, relocate certain parts to a new Article 13, consisting of new Rule 13-01 and 13-02 of Reg S-X

Financial disclosures about guarantors and issuers of guaranteed securities *(cont'd)*

Rule 3-10

- General Rule: Each issuer and each guarantor of registered debt securities must file its own, separate, audited annual and unaudited interim financial statements
- Exception: Old Rule 3-10 provides for 5 different exemptions that allow omission of separate financial statements, subject to conditions, including that:
  - Subsidiary issuer or guarantor must be "100%-owned" by parent company
  - Each guarantee must be "full and unconditional" and in case of multiple guarantees, "joint and several"
  - Parent company must provide alternative disclosures (commonly, in the form of *condensed consolidating financial information*) in its consolidated financial statement footnotes, for so long as guaranteed securities remain outstanding
- Exception based on eligible issuer-guarantor structure (*e.g.* finance or operating sub issues, with parent guaranty; parent company issues with subs guaranty)

Financial disclosures about guarantors and issuers of guaranteed securities *(cont'd)*

Amended Rule 3-10/New Rule 13-01

- Replaces condition that subsidiary be *100%-owned* by parent company with condition that it be *consolidated* in parent's consolidated financial statements
- Replaces 5 eligible structures with two broad eligible categories, *i.e.* either:
  - (**x**) parent company issues security or co-issues security, jointly and severally, with one or more of its consolidated subsidiaries or (**y**) a consolidated subsidiary issues security or co-issues security with one or more other consolidated subsidiaries of parent company, and security is guaranteed fully and unconditionally by parent company
  - So, role of parent company, not subsidiary guarantor is relevant
- Simplifies conditions to allow omission of separate financials:
  - (**1**) consolidated financial statements of parent company have been filed, (**2**) subsidiary issuer or guarantor is a consolidated subsidiary of parent company, (**3**) guaranteed security is debt or debt-like, (**4**) issuer and guarantor structure must be one of two eligible structures above, and (**5**) parent company provides Revised Alternative Disclosures

Financial disclosures about guarantors and issuers of guaranteed securities *(cont'd)*

Amended Rule 3-10/New Rule 13-01

- Replaces condensed consolidating financial information with shorter, abbreviated "Summarized Financial Information" (SFI) and non-financial disclosures that will expand qualitative disclosures about guarantees, issuers and guarantors
  - SFI includes select (instead of all major captions of) balance sheet and income statement line items and accompanying note briefly describing basis of presentation, but unlike Condensed Consolidating Information, excludes cash flow statement items
  - SFI of subsidiary issuer or guarantor may be presented on a combined basis with parent
  - Information related to subsidiaries that are not issuers or guarantors not required
  - SFI covers only most recently ended fiscal year and year-to-date interim period included in parent company's financial statements
  - Non-financial disclosures to the extent material, to include qualitative disclosures about guarantees, issuer, guarantors, and information affecting payment to holders

Financial disclosures about guarantors and issuers of guaranteed securities

Amended Rule 3-10/New Rule 13-01

- Permits the amended disclosures to be provided outside the consolidated financial statement footnotes e.g., MD&A or prominently after “Risk Factors”
- Requires amended disclosures for as long as issuer or guarantor has an Exchange Act reporting obligation with respect to guaranteed securities rather than as long as guaranteed securities are outstanding

Financial disclosures about guarantors and issuers of guaranteed securities *(cont'd)*

Rule 3-16

- Rule 3-16 requires financial statements for each affiliate the securities of which constitute a "substantial portion" of collateral for registered securities
  - Old Rule 3-16: "Substantial portion" = Value of affiliate's securities (e.g., greatest of principal amount, par value, book value or market value) equals or exceeds 20% of principal amount of securities registered

Amended Rule 3-16/New Rule 13-02

- Replaces requirement to provide affiliate financial statements with abbreviated financial and non-financial disclosures about affiliate/s and collateral arrangement as a supplement to registrant's consolidated financial statements
- Replaces "substantial portion" test with requirement to provide disclosures in all cases, unless they are immaterial
- Permits disclosures to be provided outside consolidated financial statement footnotes

Financial disclosures about guarantors and issuers of guaranteed securities *(cont'd)*

- Some practical considerations:
  - Welcome development for issuers contemplating registered debt offerings that feature these credit enhancements
  - Greater flexibility for issuers to pursue SEC-registered offering rather than Rule 144A route and seek better pricing terms
  - Makes it easier for controlled subsidiaries and joint venture entities to provide guarantees for debt securities e.g., facilitate upstream guarantees to parent company issued debt, which could enhance overall credit silo available for debt holders and avoid structural subordination issues
  - Greater flexibility for "UP-C" and "UPREIT" structures

Securities Offering Reform for BDCs and Closed-End Funds

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Treatment under the Securities Act

- The securities laws have historically distinguished between operating companies and BDCs and CEFs
- Practically, this meant that:
  - Such entities were not able to incorporate by reference in their registration statements, thus requiring the filing of post-effective amendments
  - Such entities were permitted in reliance on no action letter guidance to use Registration Statements on Form N-2 as "shelf registration statements," however, Rule 415 did not apply
  - The research safe harbors under Rules 138 and 139 did not apply to them
  - Access equals delivery was not available to them

Securities Offering and Communications Reforms

- The SEC was required to undertake rulemaking with respect to BDCs by the Small Business Credit Availability Act and to undertake rulemaking with respect to CEFs by the Economic Growth, Regulatory Relief and Consumer Protection Act
- On April 8, 2020, the SEC adopted amendments that modernize the offering related provisions of the Securities Act and the communications safe harbors
  - The amendments went effective in August 2020
  - The SEC adopted accompanying amendments to Form N-2
- The amendments streamline the registration, offering and communications processes

Securities Offering and Communications Reforms *(cont'd)*

- Among the *most important* changes are:
  - The ability to qualify as well-known seasoned issuers (WKSIs) to the extent that the BDC/CEF meets the reporting history and public float requirements;
  - To benefit as WKSIs from the ability to engage in certain communications and rely on expedited shelf registration provisions;
  - The ability for other (non-WKSI) BDCs/CEFs to use streamlined shelf registration statement procedures; and
  - The ability to rely on a number of important communications safe harbors

Shelf Registration Process

- BDCs/CEFs are now able to engage in a streamlined registration process to sell securities "off the shelf" more quickly and efficiently through the use of a short-form registration statement
- BDCs/CEFs are now eligible to use the short-form registration statement if:
  - They meet the registrant requirements of General Instruction 1.A. of Form S-3, which requires that the issuer have a class of securities registered under the Exchange Act or be required to file reports under the Exchange Act, been subject to the Exchange Act reporting requirements and filed all required Exchange Act reports for at least 12 months preceding the filing of the registration statement, and timely filed all required Exchange Act reports during the 12 months preceding the filing of the registration statement and meet the transaction requirements of General Instruction 1.B. or 1.C. of Form S-3, and, for primary offerings, have greater than $75 million of market value of outstanding common equity held by non-affiliates

Shelf Registration Process *(cont'd)*

- These entities are referred to as Seasoned Funds
- Seasoned Funds are now permitted to use a short-form registration statement on Form N-2 (pursuant to new General Instruction A.2 in Form N-2) similar to a Form S-3 registration statement
- A qualifying BDC/CEF that files this short-form registration statement can use it to register shelf offerings, including shelf registration statements that are filed by entities that qualify as WKSIs and become effective automatically, and can satisfy Form N-2's disclosure requirements by incorporating by reference information from the entity's periodic public reports (backward incorporation) as well as by incorporating by reference into the registration statement subsequently filed Exchange Act reports (forward incorporate)

WKSI Status

- A BDC/CEF is able to qualify as a WKSI and file an automatically effective shelf registration statement on Form N-2 and avail itself of other benefits to which WKSIs are entitled
- The SEC did not modify or tailor the $700 million public float WKSI test as many commenters had suggested to the SEC
  - Nonetheless, many BDCs/CEFs already have the common equity market value necessary to meet the WKSI criteria
- Qualifying entities are now able to promptly take advantage of favorable conditions in the public market

WKSI Status

- An entity that is a WKSI is able to:
  - Register an unspecified amount of different types of securities
  - Benefit from pay-as-you-go for registration fees
  - Engage in a broader range of communications

Omission of Information from a Base Prospectus or Prospectus Supplement

- Like any operating company, a BDC/CEF is now able to rely on Rule 430B, which allows for the omission of information from a base prospectus that is not known at the time of effectiveness
- A WKSI is able to omit the plan of distribution from their registration statements and omit information as to whether the offering is a primary offering or a secondary offering
- A Seasoned Fund is able to omit certain information from their registration statements
- A BDC/CEF also is able to rely on Rule 424 to file prospectus supplements, like operating companies; the Rule 424 standard is less burdensome than the Rule 497 standard

Access Equals Delivery

- Rules 172 and 173, which permit “access equals delivery,” is now applicable to BDCs/CEFs
- The prospectus and incorporated materials are required to be made available on the entity’s website
- This eliminates the outdated process of having to print prospectuses and deliver physical copies of prospectuses to investors in BDC/CEF offerings

Communication Rules

- BDCs/CEFs are now able to rely on various communications safe harbors under the Securities Act, including the following:
  - Rules 168 and 169 under the Securities Act, which allow Exchange Act-reporting and non-reporting companies to disseminate regularly released factual business and forward-looking information even around the time of a securities offering
  - Rule 134, which provides a safe harbor that allows issuers to make certain written statements regarding an offer after a prospectus is filed
  - Rule 163A, which provides a safe harbor from the Section 5(c) prohibition on pre-filing offers for communications that do not reference an offering, and that are made more than 30 days prior to the filing of a registration statement
  - Rule 163, which provides a safe harbor from the Section 5(c) prohibition on pre-filing offers for WKSIs to engage in unrestricted oral and written communications before the filing of a registration statement

Communications Rules *(cont'd)*

- BDCs/CEFs also are able to produce free writing prospectuses under Rule 433
- Broker-dealers that participate in a registered offering may rely on the safe harbor in Rule 138 in connection with publishing research reports
- The SEC did not amend Rule 139 (the non-exclusive safe harbor for issuer-specific research reports)
- As a result of a different statutory mandate, the SEC already had amended this safe harbor, by adopting Rule 139b, which provides a safe harbor for certain covered fund research reports

Disclosure Requirements

- A Seasoned Fund that files a shelf registration statement is required to include the following information in their annual reports:
  - The fee and expense table that is a part of Form N-2
  - The share price data required by Form N-2
  - The senior securities table required by Form N-2
  - A Seasoned Fund also is required to disclose in its registration statement or annual report any unresolved comments
- BDCs/CEFs also are required to make incorporated documents available on a website

Amendments to Financial Disclosures about Acquired Businesses

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Amendments to financial disclosures about acquired businesses

- On May 21, 2020, the SEC amended financial disclosure rules with respect to business acquisitions required by Rule 3-05 and Article 11 of Regulation S-X
- Aims to improve financial information available to investors about acquired or disposed businesses, facilitate more timely access by issuers to capital, reduce complexity and costs to prepare disclosures
- Effective Date: January 1, 2021
- Amendments revise Rules 3-05 (financial statements of acquired businesses), 3-14 (real estate operations), Article 11 (pro forma financial information), other related rules of Reg S-X

Background

- Rule 3-05 requires audited annual and unaudited interim financial statements to be provided if a significant acquisition has occurred or is probable, and the business acquired or to be acquired would be considered a significant subsidiary under Rule 1-02(w) of Reg. S-X, substituting 20% for the 10% trigger threshold in that rule
- Rule 11-01 of Reg. S-X requires unaudited annual and interim pro forma financial statements if a significant acquisition has occurred or is probable, looking to the same tests in Rule 1-02(w) for determining whether a business acquisition is significant
- Rule 1-02(w) contains three tests for determining whether a subsidiary or business combination is significant – investment test, asset test, income test. Under Old Rule:

Investment Test	Asset Test	Income Test
$\frac{\text{Purchase Price}}{\text{Buyer's Total Assets}}$	$\frac{\text{Target's Total Assets}}{\text{Buyer's Total Assets}}$	$\frac{\text{Target's Pre-Tax Income}}{\text{Buyer's Pre-Tax Income}}$

Revised Investment Test

- Investment Test has been revised:
  - For acquisitions . . . and dispositions this test is met when the registrant's and its other subsidiaries' investments in and advances to the tested subsidiary exceed 10% of the aggregate worldwide market value of the registrant's voting and non-voting common equity, or if the registrant has no such aggregate worldwide market value the total assets of the registrant and its subsidiaries consolidated as of the end of the most recently completed fiscal year
  - When determining the aggregate worldwide market value of the registrant's voting and non-voting common equity, use the average of such aggregate worldwide market value calculated daily for the last five trading days of the registrant's most recently completed month ending prior to the earlier of the registrant's announcement date or agreement date of the acquisition or disposition

Revised Investment Test

- Changes to the Old Rule:
  - Replaces denominator with aggregate worldwide market value of voting and non-voting common equity for total assets when the registrant has a market value for its voting and non-voting common equity
    - If there is no aggregate worldwide market value, then use the denominator in Old Rule
  - Requires inclusion of fair value of any contingent consideration in calculating investments in or advances to the tested subsidiary unless likelihood of payment is remote

Investment Test (Old Rule)	**Investment Test (New Rule)**
$\frac{\text{Purchase Price}}{\text{Buyer's Total Assets}}$	$\frac{\text{Purchase Price}}{\text{Buyer's Aggregate Worldwide Market Value of Common Equity}}$

Revised Income Test

- Income Test has been revised to add a revenue component. The test is met if:
  - The absolute value of the registrant's and its other subsidiaries' equity in the tested subsidiary's consolidated income or loss from continuing operations before income taxes (after intercompany eliminations) attributable to the controlling interests exceeds 10% of the absolute value of such income or loss of the registrant and its subsidiaries consolidated for the most recently completed fiscal year; and
  - The registrant's and its other subsidiaries' proportionate share of the tested subsidiary's consolidated total revenue from continuing operations (after intercompany eliminations) exceeds 10% of such total revenue of the registrant and its subsidiaries consolidated for the most recently completed fiscal year. This component does not apply if either the registrant and its subsidiaries consolidated or the tested subsidiary did not have material revenue in each of the two most recently completed fiscal years

Revised Income Test

- Changes to the Old Rule:
  - Adds a revenue test that must be satisfied in addition to the income test
  - Both the revenue test and the income test thresholds must be exceeded for the income test to be met
  - The revenue test does not apply if either the registrant or the tested subsidiary did not have material revenue in either of the previous two years
  - Loss years reflected at absolute value rather than a zero

Income Test (Old Rule)	**Income Test (New Rule)**
$\frac{\text{Target's Pre-Tax Income}}{\text{Buyer's Pre-Tax Income}}$	The ***lower*** of: $\frac{\text{Target's Pre-Tax Income}}{\text{Buyer's Pre-Tax Income}}$ **and** $\frac{\text{Target's Revenue}}{\text{Buyer's Revenue}}$

Audited Financial Statements for Significant Subsidiaries

- Amended Rules require up to two years of Rule 3-05 Financial Statements
  - Previously, three years required if a significance test exceeded 50%
  - Third year eliminated because less likely to be indicative of current condition and results while adding significant incremental cost
- Where a significance test exceeds 20% but none exceeds 40% financial statements are required for the "most recent" interim period specified in Rule 3-01 and 3-02
  - As opposed to "any" interim period
  - Eliminates need for comparative interim period where only one year of audited Rule 3-05 Financial Statements required
- Rule 4-01(a) requires further material information as necessary to make required statements not misleading

Periods for Rule 3-05 Financial Statements

PERIODS TO BE PRESENTED	
Significance Level	**Required Financial Periods**
If all significance tests less than 20%	No Rule 3-05 Financial Statements required
If any significance test greater than 20% but none exceed 40%	One year of audited financial statements; unaudited financial statements for most recent interim period (but no corresponding prior year interim period)
If any significance test greater than 40%	Two years of audited financial statements and unaudited financial statements for most recent, and corresponding prior year, interim period

Pro Forma Information to Measure Significance

- Filed pro forma financial information that only depicts significant business acquisitions and dispositions consummated after the latest fiscal year-end may be used to measure significance, if:
  - Rule 3-05 Financial Statements (or, for real estate operations, Rule 3-14 Financial Statements) have been filed for any such acquired business, and
  - Pro forma financial information required by Article 11 for any such acquired or disposed business has been filed
- Pro forma financial information used to measure significance may only give effect to the subsequently acquired or disposed business
- Pro forma information used to measure significance may not give effect to Autonomous Entity Adjustments, Management's Adjustments, or other transactions, such as the use of proceeds from an offering
- Once a registrant uses pro formas to measure significance, it must continue to use pro formas to measure significance until the next annual report on Form 10-K or Form 20-F

Individually Insignificant Acquisitions

- The Amended Rules clarify that "individually insignificant businesses" include:
  - Any acquisition consummated after the registrant's audited balance sheet date whose significance does not exceed 20%,
  - Any probable acquisition whose significance does not exceed 50%, and
  - Any consummated acquisition whose significance exceeds 20%, but does not exceed 50%, for which financial statements are not yet required because of the 75-day filing period.
- Pre-acquisition historical financial statements only for those businesses whose individual significance exceeds 20%
- Pro forma financial information depicting the aggregate effects of all "individually insignificant businesses" in all material respects
- Exception permitting pro forma financial information not to be provided does not apply where the aggregate impact is significant

Pro Forma Financial Information Adjustments

- Amendments to Article 11 of Reg S-X modify criteria for pro forma adjustments and provide three new categories of permitted adjustments
- Adjustment criteria for pro forma financial information requirements broken out into three categories:
  - "Transaction Accounting Adjustments" which reflect only the application of required accounting to the transaction
  - "Autonomous Entity Adjustments" which reflect the operations and financial position of the registrant as an autonomous entity if it was previously part of another entity, and
  - Optional "Management's Adjustments" depicting synergies and dis-synergies of acquisitions and dispositions for which pro forma effect is being given if, in management's opinion, such adjustments enhance understanding of the pro forma effects of the transaction
    - As a condition for presenting Management's Adjustments, certain conditions related to the basis and form of presentation must be met

Transactional Accounting and Autonomous Entity Adjustments

- Transactional Accounting Adjustments must depict:
  - In the pro forma condensed balance sheet, the accounting for the transaction required by U.S. GAAP or IFRS-IASB, as applicable, and
  - In the pro forma condensed income statements, the effects of those pro forma balance sheet adjustments assuming the adjustments were made as of the beginning of the fiscal year presented
  - If no balance sheet effect, then the Transaction Accounting Adjustments to the pro forma statement of comprehensive income should depict the accounting for the transaction required by U.S. GAAP or IFRS-IASB, as applicable
- Autonomous Entity Adjustments
  - Pro forma per share data must give effect to Autonomous Entity Adjustments
  - Must be presented in a separate column from Transaction Accounting Adjustments

Basis for Management's Adjustments

- Management's Adjustments must satisfy the following conditions:
  - There must be a reasonable basis for each such adjustment
  - The adjustments are limited to the effect of such synergies and dis-synergies on the historical financial statements that form the basis for the pro forma statement of comprehensive income as if the synergies and dis-synergies existed as of the beginning of the fiscal year presented
    - If such adjustments reduce expenses, the reduction can't exceed the amount of the related expense historically incurred during the pro forma period presented
  - The pro forma financial information must reflects all Management's Adjustments that are, in the opinion of management, necessary to a fair statement of the pro forma financial information presented
    - A statement to that effect must be disclosed
    - When synergies are presented, any related dis-synergies shall also be presented

Practical Considerations

Financial disclosures re acquired businesses

The Amended Rules:

- Ease burdens and costs involved in preparation of financial statements
  - Maximum of two (instead of three) years of audited annual financials
  - Corresponding prior year interim period required only at more than 40% significance
  - Increased significance threshold for dispositions from 10% to 20%
  - Permit abbreviated financials for acquisitions of a component of an entity
  - Allow omission of target financials once business included in registrant's post-acquisition financial statements for nine months or one year
  - Eliminated required three years of audited annual financials if real estate operation acquired from a related party
  - Allow presentation of Rule 3-05 Financial Statements of Foreign Businesses or Foreign Private Issuers in accordance with IFRS-IASB without reconciliation to U.S. GAAP

Practical Considerations

Financial disclosures re acquired businesses *(cont'd)*

The Amended Rules:

- Assist registrants make more meaningful significance determinations
  - Using aggregate worldwide market value for investment test corrects fair value vs. book value mismatch in investment test under Old Rule
  - Adding revenue component to income test prevents anomalous results, especially for registrants with net loss or low net income
- Introduce new obligations and challenges for registrants
  - Management's Adjustments, while optional, require management to present reasonably estimable synergies and dis-synergies of the acquisition and to have a reasonable basis for each adjustment
    - Requires management to state that pro formas reflect all Management's Adjustments that are, in their opinion, necessary to a fair statement of pro formas
  - Registrants will need to get used to presenting pro formas under Amended Rules, including presentation of "Transaction Accounting Adjustments," "Autonomous Entity Adjustments" and related explanatory notes

Practical Considerations

Financial disclosures re acquired businesses *(cont'd)*

A few practical reminders and tips for reporting companies:

- Assess how Amended Rules impact your disclosures
  - Public companies that engage or are considering engaging, in acquisitions or dispositions should involve their accounting departments and counsel
- Pay attention to the SEC's reminder that financial disclosures must be complete and not misleading:
  - "*In adopting these changes, we note that regardless of the number of years presented, if trends depicted in Rule 3-05 Financial Statements are not indicative or are otherwise incomplete, 17 CFR 210.4-01(a) ('Rule 4-01(a)') requires that a registrant provide 'such further material information as is necessary to make the required statements, in light of the circumstances under which they are made, not misleading.'*"
- Remember that Rule 3-13 waiver requests are available and can be utilized by registrants

Amending the "Accredited Investor" Definition

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Amending the "Accredited Investor" Definition

- On August 26, 2020, the SEC adopted amendments to the definition of "accredited investor" and related amendments to the definition of "qualified institutional buyer."
- The adopting release reaffirms the existing aspects of the definition that an accredited investor includes a person who meets one of the listed qualification methods.
- The amendments supplement the existing definition by adding two new categories of accredited investors for natural persons, regardless of such person's income or net worth.

New Categories for Natural Persons

- The first added category allows a natural person to qualify as an accredited investor, regardless of net income or net worth, if the person holds certain professional certifications, designations or credentials
- The second added category allows knowledgeable employees to qualify as accredited investors for purposes of investing in the funds sponsored by their employers.
- The final amendments clarify that, in calculating income and net worth, as well as in the context of knowledgeable employee joint investments, an investor can aggregate the investor's income or net worth, as the case may be, with that of his or her spouse or spousal equivalent.

New Categories for Institutions

- The amendments also add several new categories of entities to the accredited investor definition, including:
  - SEC- and state-registered investment advisers.
  - Rural business investment companies.
  - Limited liability companies (or any similar business entity) that satisfy the other requirements of the definition of "accredited investor" (i.e., total assets in excess of $5 million and not formed for the specific purpose of acquiring the securities being offered).
  - Any entity that does not otherwise qualify as an accredited investor owning investments as defined in Rule 2a51-1(b) under the Investment Company Act in excess of $5 million that is not formed for the specific purpose of acquiring the securities being offered.
  - Any family office with at least $5 million in assets under management

Qualified Institutional Buyer Definition

- The SEC also amended the definition of qualified institutional buyer in Rule 144A to avoid inconsistencies and include the entities that qualify as institutional accredited investors when these entities meet the $100 million in securities owned and invested threshold in Rule 144A.

Exempt Offering Framework Amendments

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Exempt offering framework amendments

- The amendments address:
  - The integration framework
  - Demo day communications
  - Generic solicitations of interest
  - Amendments to Rule 506
  - Harmonize disclosure and bad actor requirements
  - Amend the offering thresholds and investment limits for Regulation A, Regulation Crowdfunding (CF), and Rule 504
  - Amend the eligibility criteria for Reg A and Reg CF

Guiding Principles for Integration Analysis

- Rule 152(a) sets out the general principle, which provides that for all offerings not covered by one of the safe harbors contained in Rule 152(b), offers and sales will not be integrated if, based on the particular facts and circumstances, the issuer can establish that each offering either complies with the registration requirements of the Securities Act, or an exemption from registration that is available for the particular offering.
- Rule 152(a)1) codifies the SEC guidance from 2007 and the Staff interpretations and relates to exempt offerings as to which general solicitation is not permitted. In this case, the issuer must have a reasonable belief, based on the facts and circumstances, with respect to each purchaser in the exempt offering prohibiting general solicitation, that the issuer (or any person acting on the issuer's behalf) either (**1**) did not solicit such purchaser through the use of general solicitation; or (**2**) established a substantive relationship with such purchaser prior to the commencement of the exempt offering prohibiting general solicitation.
- Rule 152(a)(2), addresses two or more concurrent exempt offerings permitting general solicitation. In this case, the issuer's general solicitation offering materials for one offering that includes information about the material terms of a concurrent offering under another exemption may constitute an "offer" of the securities in such other offering.
- In addition to satisfying the conditions of the particular exemption, the offer must comply with all the requirements for, and restrictions on, offers under the exemption being relied on for such other offering, including any necessary legends or communications restrictions.

Non-exclusive integration safe harbors

New Rule 152(b) provides the four non-exclusive integration safe harbors shown below:

Safe Harbor 1, Rule 152(b)(1)	Any offering made more than 30 calendar days before the commencement of any other offering, or more than 30 calendar days after the termination or completion of any other offering, would not be integrated with such other offering; provided, that, for an exempt offering for which general solicitation is not permitted that follows by 30 calendar days or more an offering that allows general solicitation, the provisions of Rule 152(a)(1) apply (i.e., the purchasers either were not solicited through the use of general solicitation or established a substantive relationship with the issuer prior to the commencement of the offering for which general solicitation is not permitted).
Safe Harbor 2, Rule 152(b)(2)	Offers and sales made in compliance with Rule 701, pursuant to an employee benefits plan, or in compliance with Regulation S would not be integrated with other offerings.
Safe Harbor 3, Rule 152(b)(3)	An offering for which a Securities Act registration statement has been filed would not be integrated if made subsequent to: (1) a terminated or completed offering for which general solicitation is not permitted; (2) a terminated or completed offering for which general solicitation is permitted and made only to qualified institutional buyers (QIBs) and institutional accredited investors (IAIs), or (3) an offering for which general solicitation is permitted that terminated or completed more than 30 calendar days prior to the commencement of the registered offering.
Safe Harbor 4, Rule 152(b)(4)	Offers and sales made in reliance on an exemption for which general solicitation is permitted would not be integrated if made subsequent to any terminated or completed offering.

Amendments to Rule 506(b)

- Modify Rule 506(b) to limit number of non-accredited investors that may participate in such offerings to no more than 35 within a 90-calendar-day period
- Designed to prevent issuers from using the new 30-day integration safe harbor to conduct a distribution of securities to 35 unique non-accredited investors every month

New General Solicitation Carve Out for Demo Day Communications

- New Rule 148 provides that certain "demo day" communication will not be deemed to constitute a general solicitation for purposes of Rule 506(b)
- An issuer will not be deemed to have engaged in general solicitation if the communications are made in connection with a seminar or meeting sponsored by a college, university, or other institution of higher education, a State or local government, a nonprofit organization, or an angel investor group, incubator or accelerator
- New rule limits information conveyed at the event regarding the offering of securities by or on behalf of the issuer to the following:
  - Notification that issuer is in the process of offering or planning to offer securities;
  - Type and amount of securities being offered;
  - Intended use of the proceeds of the offering; and
  - Unsubscribed amount in an offering.

New General Solicitation Carve Out for Demo Day Communications *(cont'd)*

- New rule requires that more than one issuer participate in the event and that the event sponsor not be permitted to:
  - Make investment recommendations or provide investment advice to attendees of the event;
  - Engage in any investment negotiations between the issuer and investors attending the event;
  - Charge attendees of the event any fees, other than reasonable administrative fees;
  - Receive any compensation with respect to the event that would require it to register as a broker or dealer under the Securities Exchange Act of 1934, as amended (Exchange Act), or as an investment adviser under the Investment Advisers Act of 1940.
- Online participation in the event must be limited to:
  - individuals who are associated with the sponsor;
  - individuals that the sponsor reasonably believes are accredited investors; or
  - individuals who have been invited to the event based on industry or investment-related experience reasonably selected by the sponsor in good faith and disclosed in the public communications about the event.

Amendments to Rule 506(c)

- Rule 506(c) permits issuers to generally solicit and advertise an offering, so long as the issuer takes reasonable steps to verify that all purchasers in the offering are accredited investors
- Amendments add new item to the non-exclusive list in Rule 506(c) that allows an issuer to establish that an investor for which the issuer previously took reasonable steps to verify status as an accredited investor remains an accredited investor as of the time of a subsequent sale if the investor provides a written representation to that effect and the issuer is not aware of information to the contrary
- In a change from the proposed amendments, the SEC added a five-year time limit in the final rule on the ability of the issuer to rely on the earlier verification

Harmonization of Reg D Disclosure Requirements

- For Reg D offerings by non-reporting companies that include non-accredited investors, the disclosure requirements have been aligned with those required in Regulation A offerings
- Reg D offerings of up to $20 million in securities, issuer must comply with the requirements of paragraph (b) of part F/S of Form 1-A, which applied to Tier 1 Regulation A offerings
- Reg D offerings of greater than $20 million in securities, issuer must provide audited financial statements and comply with the requirements of Regulation S-X similar to Tier 2 Regulation A offerings
- Issuer must furnish the non-financial statement information required by Part II of Form 1-A (if the issuer is eligible to use Regulation A) or Part I of a Securities Act registration statement on a form that the issuer would be eligible to use
- Reporting issuer must furnish its annual report to shareholders for the most recent fiscal year and the definitive proxy statement filed in connection with the annual report, or the most recently filed annual report on Form 10-K or registration statement
- Foreign private issuer that is not an Exchange Act reporting company would be required to provide financial statement disclosure consistent with the Regulation A requirements, either prepared in accordance with U.S. GAAP or IFRS as issued by the IASB

New Generic Solicitations of Interest Relating to Potential Exempt Offerings

- New Rule 241 provide an exemption for generic solicitations of interest
- An issuer (or a person authorized to act on the issuer's behalf) may engage in efforts to determine whether there is interest in a contemplated exempt offering of securities without deciding what exemption is being relied upon ahead of time
- No solicitation or acceptance of any commitment, binding or otherwise, from any person will be permitted until the issuer makes a determination as to the exemption on which it intends to rely.
- Rule 241 requires the generic testing-the-waters materials to provide specified disclosures notifying potential investors about the limitations of the generic solicitation. The materials must state that:
  - The issuer is considering an offering of securities exempt from registration, but has not determined a specific exemption from registration the issuer intends to rely on for the subsequent offer and sale of the securities;
  - No money or other consideration is being solicited, and if sent in response, will not be accepted;
  - No offer to buy the securities can be accepted, no part of the purchase price can be received until the issuer determines the exemption under which the offering is intended to be conducted, and, where applicable, the filing, disclosure or qualification requirements of such exemption are met; and
  - A person's indication of interest involves no obligation or commitment of any kind.

New Generic Solicitations of Interest Relating to Potential Exempt Offerings *(cont'd)*

- Additionally, issuer must provide purchasers with any written materials used under new Rule 241 if the issuer sells securities under Rule 506(b) within 30 days of the generic solicitation of interest to any purchaser that is not an accredited investor
- Rule 241 generic solicitation materials must be made publicly available as an exhibit to the offering materials filed with the SEC in connection with a Reg A or Reg CF offering commenced within 30 days of the generic solicitation

Changes to Offering Exemption

- The SEC broadened certain of the existing exemptions in a number of ways
- Offering limits
- The amounts that may be offered under the three capital-raising exemptions that currently are capped are increased as follows:
  - The Regulation A Tier 2 primary offering limit is increased from $50 million to $75 million and the secondary sales limit is increased from $15 million to $22.5 million. No change is made in the Tier 1 limits, which remain at $20 million for a primary offering and $6 million for a secondary offering.
  - The Regulation Crowdfunding limit is increased from $1.07 million to $5 million.
  - The Regulation D Rule 504 limit is increased from $5 million to $10 million.

Crowdfunding Investor Limits

- The investment limits for investors in Regulation Crowdfunding offerings are loosened by eliminating those limits for accredited investors and by allowing non-accredited investors to rely on the greater of their annual income or net worth in calculating the limit. That limit is in any 12-month period through a crowdfunding offering:
  - the greater of $2,200 or 5% of the greater of annual income or net worth, if either is less than $107,000, or
  - 10% of the greater of annual income or net worth, but not more than $107,000, if both are at least $107,000.
- The opportunities to use Regulation Crowdfunding also are expanded by permitting special purpose crowdfunding vehicles that pool investments to be investors without being classified as an "investment company."

Modernization of Regulation S-K

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Amendments to S-K Item 105 Risk Factor Disclosure

As part of the SEC modernization amendments to Regulation S-K adopted this past August, the amendments to Item 105 regarding risk factors were adopted:

- Requirement of a summary of not more than two pages in the "forepart" of the annual report if the discussion exceeds 15 pages;
- Change to the disclosure standard from "most significant" risks to "material" risks;
- Required organization of risks under relevant headings; and
- Requirement that generic risks (not specifically relevant to a company's investors) be placed at the end of the discussion under a heading entitled "General Risk Factors".

Business Description (Item 101(c))

In addition to the amendment to the general approach to the business disclosure requirements of S-K, the requirements for this Item have several notable specific amendments.

- New Human Capital Disclosure;
  - The company's human capital resources; and
  - Human capital resources that the company focuses on in managing its business.
- Government Regulations – not just environmental anymore; and
- Other Prescriptive Disclosure Items – any item that is material to investment and voting decisions, rather than current quantitative thresholds.

Legal Proceedings (Item 103)

The amendments to legal proceedings disclosure also raise the threshold for disclosure of environmental proceedings to which a governmental authority is a party from $100,000 to $300,000, with the flexibility for the company to select a different threshold so long as such threshold:

- Is reasonably designed to disclose any material proceeding;
- Does not exceed the lesser of (**i**) $1 million or (**ii**) 1% of the current assets of the company and its subsidiaries on a consolidated basis; and
- Is disclosed, together with any changes, in **each** annual **and** quarterly report.

SEC Transitional FAQs re Items 101 and 103

On November 5, 2020, the Staff issued FAQs with respect to the amendments to modernize Regulation S-K with the following points of clarification:

- For prospectus supplements filed after November 9 for registration statements effective prior to November 9, issuers don't need to comply with new Items 101 and 103 or amend the 10-K currently incorporated by reference in the registration statement to comply with the amended Items 101 and 103.

  In addition, although 401(a) requires a prospectus supplement conform to applicable rules on the initial file date of the supplement and Item 3 of Form S-3 expressly requires Item 105 disclosure, the Staff has stated that it will not object if the prospectus supplement complies with previous Item 105 until the next update to the registration statement for Section 10(a)(3) purposes.
- The amendments don't require 10-K disclosure of new 101 business developments for more than the fiscal year covered by the current 10-K.

SEC Transitional FAQs re Items 101 and 103 *(cont'd)*

- A registrant may omit the full discussion of the general development of its business in a 10-K or registration statement if the registrant:
  - Discloses all material developments since the most recent report or registration that included the full discussion;
  - Includes a hyperlink to the report or registration statement that included the full disclosure; and
  - Incorporates the full discussion by reference to the report or registration statement.

  The Staff has stated that it anticipates that this updating method will apply mainly to registration statements.

Amendments to MD&A of Financial Condition and Results of Operations

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Amendment to MD&A and Related Disclosures

- On November 19, 2020, the SEC
  - Amended Item 303 of Regulation S-K (Management's Discussion and Analysis of Financial Condition and Results of Operations or MD&A) and
  - Revised or eliminated several other requirements of Regulation S-K
- The SEC adopted these changes to
  - To eliminate duplicative disclosures and
  - Modernize and enhance MD&A disclosures for the benefit of investors, while simplifying compliance efforts for registrants.

Effective and Compliance Dates

- Effective Date
  - **February 10, 2021**
- Mandatory Compliance Date
  - Beginning with first fiscal year ending on or after the date August 9, 2021
  - Companies must apply the amended rules in a registration statement and prospectus that on its ***initial filing date*** is required to contain financial statements for a period on or after the mandatory compliance date.
- Voluntary Early Compliance
  - Allowed at any time after the effective date as long as disclosure is responsive to an amended item in its entirety.

New paragraph 303 (a) – Objective

- New paragraph (a) to Item 303 clarifies the objective of MD&A by incorporating much of current Instructions 1, 2 and 3
  - Emphasizes the objective of MD&A for both full fiscal years and interim periods.
  - Disclosure generally is expected to better allow an investor to view the company from management's perspective.
  - Current Items 303(a) and (b) have been recaptioned as Items 303(b) and (c), respectively

Capital Resources (reflected in new Item 303(b)(1) and Item 303(b)(1)(ii))

- Disclosure of material cash requirements, including
  - Commitments for capital expenditures,
  - Anticipated source of funds needed to satisfy these cash requirements, and
  - General purpose of the cash requirements
- The objective is to account for capital expenditures that are not necessarily capital investments, such as
  - Human capital or intellectual property
- Product lines may need to be discussed where necessary to understand a company's business.

Results of Operations (reflected in Item 303(b)(2)(ii)

- Companies must disclose known events that are reasonably likely to cause a material change in the relationship between costs and revenues, such as known or reasonably likely future increases in
  - Costs of labor or materials
  - Price increases
  - Inventory adjustments
- Companies must disclose the reasons underlying material changes in net sales or revenues

Results of Operations (reflected in Item 303(b)(2)(ii) *(cont'd.)*

- Elimination of specific disclosure with respect to the impact of inflation and changing prices.
  - Companies will still be required to discuss these matters if they are part of a known trend or uncertainty that has had, or is reasonably likely to have, a material impact on net sales or revenue.
  - This will allow companies to focus on material disclosure that is tailored to their business, facts and circumstances.

Off Balance Sheet Arrangements

- Current requirement eliminated
- Companies should consider off-balance sheet arrangements within the broader context of their MD&A
- Instruction 8 requires companies to discuss commitments and obligations arising from arrangements with unconsolidated entities or persons that have, or are reasonably likely to have, a material current or future effect on their:
  - Financial condition,
  - Changes in financial condition,
  - Revenues or expenses,
  - Results of operations,
  - Liquidity,
  - Cash requirements, or
  - Capital resources.

Tabular Disclosure of Contractual Obligations

- Eliminated this disclosure requirement currently in paragraph (a)(5)
- Amended Item 303(b) requires disclosure of material cash requirements from known contractual and other obligations as part of a liquidity and capital resources discussion
- The adopting release explains that the "amendments are intended to focus only on material disclosures and specifically, disclosure of those periods where the cash requirements or reasonably likely effect of these cash requirements on liquidity and capital resources is material."

Line Item Changes and Critical Accounting Estimates

- If line item material changes, disclose the underlying reasons for these material changes in quantitative and qualitative terms
- Disclosure of critical accounting estimates explicitly required
  - Qualitative and quantitative information necessary to understand
    - The estimation uncertainty
    - Impact the critical accounting estimate has or is reasonably likely to have on financial condition or results of operations

Quarterly Periods (reflected in new Item 303(c)

- Companies can compare their most recently completed quarter to either
  - The corresponding quarter of the prior year or
  - The immediately preceding quarter
- If comparison from the prior interim period comparison changes
  - Explain the reason for the change and
  - Present both comparisons in the filing where the change is announced

Supplementary Financial Information and Selected Financial Data

- S-K Item 301 (Selected Financial Data) eliminated
- S-K Item 302 (Supplementary Financial Information) amended
  - Replaced requirement to provide two years of tabular selected quarterly financial data with a principles-based requirement requiring disclosure only when there are one or more specified retrospective changes that that, individually or in the aggregate, are material
  - Disclosure could involve a single quarter in which the material retrospective change applies, or it may flow through to subsequent quarters during the relevant look-back period

Amendments to Rule 14a-8 Regarding Shareholder Proposals

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Amendments to Rule 14a-8

- Submission threshold updated
  - Range of amount voting securities/holding period, with aggregation prohibited
- Administrative requirements, including availability to meet
- Resubmission threshold updated
  - Increased levels of support to be resubmitted at company's future meetings
- One person/one proposal clarified
  - Cannot submit multiple proposals for the same meeting, whether as a shareholder or as a representative of other shareholder(s)
- Amendments do not apply to 2021 shareholder meetings

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Click here *to access the following alerts*

- On Point: Target and Pro Forma Financial Statement Requirements for Significant Acquisitions
- SEC Amends Financial Disclosure Requirements in Registered Debt Offerings Involving Guaranteed or Collateralized Securities
- SEC Adopts Securities Offering & Communications Reforms for BDCs and Closed-End Funds
- SEC Amends Business Acquisition and Disposition Disclosure Rules
- SEC Adopts Amendments to Accredited Investor Definition
- SEC Amends Business, Legal Proceedings and Risk Factor Disclosures
- SEC Amends Shareholder Proposal Rule
- Exempt Offering Framework Amendments
- SEC Adopts Significant Changes to MD&A & Related Disclosures

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