

Taking the FAST Track: New Legislation Facilitates Raising Capital and Aims to Simplify Reporting

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Companies and members of the investment community would be forgiven for not reading all 490 pages of the Fixing America's Surface Transportation Act (the "FAST Act"), which was signed into law on December 4, 2015.¹ The FAST Act primarily deals with transportation and infrastructure funding. However, the act also includes provisions that, among other things:

- create a new exemption from registration under the Securities Act of 1933 (the "Securities Act") for private resales of securities;
- build upon the 2012 Jumpstart Our Business Startups Act (the "JOBS Act") to add additional flexibility for initial public offerings by emerging growth companies; and
- direct the SEC to simplify public company reporting requirements.

New Exemption for Resales (*effective immediately*)

The FAST Act creates a new, non-exclusive statutory exemption from Securities Act registration requirements for private resales to accredited investors. This exemption, set forth in Section 4(a)(7) of the Securities Act, applies some of the principles of the so-called "Section 4(a)(1½)" exemption that has developed over time in reliance on case law and SEC guidance. The new section, however, contains some notable features that will limit its utility.

Under Section 4(a)(7), a resale of securities is exempt from registration as long as:

- all purchasers are "accredited investors," as defined in Rule 501 of Regulation D under the Securities Act;
- the seller and any person acting on its behalf do not engage in a general solicitation or general advertising to offer or sell the securities;
- for sales of securities of a non-reporting issuer (except one that is a Schedule B foreign government or exempt from reporting pursuant to Rule 12g3-2(b) under the Securities Exchange Act of 1934 (the "Exchange Act")), the seller makes available to prospective purchasers certain information about the issuer, including, among other things:
 - a statement of the nature of the issuer's business;
 - the names of its officers and directors;
 - information about any person being paid a commission or fee in connection with the offering;

¹ The full text of the FAST ACT can be accessed at <https://www.gpo.gov/fdsys/pkg/BILLS-114hr22enr/pdf/BILLS-114hr22enr.pdf>. Appendix A to this alert provides FAST Act section references for the specific topics discussed herein.

- certain financial information about the issuer, including its balance sheet and profit and loss statement for the most recent period and for the two preceding fiscal years; and
 - to the extent that the seller is a control person with respect to the issuer, a brief statement regarding the nature of the affiliation, and a statement certified by the seller that it has no reasonable grounds to believe that the issuer is in violation of the securities laws or regulations.²
- the offering is not conducted by the issuer or a subsidiary of the issuer;
 - neither the seller nor any person receiving remuneration in connection with the transaction would be disqualified as a “bad actor” under Rule 506(d)(1) of Regulation D or under Section 3(a)(39) of the Exchange Act;
 - the issuer is engaged in business and is not in the organizational stage or in bankruptcy or receivership and is not a blank check, blind pool or shell company with no specific business plan or purpose;
 - the offering does not involve securities that are part of an unsold allotment to an underwriter of the securities; and
 - securities of the same class as the securities offered have been authorized and outstanding for at least 90 days.

Section 4(a)(7) does not impose any holding period requirement upon the seller before the securities may be sold. However, securities sold pursuant to the Section 4(a)(7) exemption will be “restricted securities,” as defined by Rule 144 under the Securities Act, in the hands of the purchaser. As a result, subsequent resales by the purchaser will remain subject to the Rule 144 holding period requirements and other restrictions and, if the Section 4(a)(7) seller is an affiliate of the issuer, will be subject to a newly commenced holding period before Rule 144 becomes available.

Also, Section 4(a)(7) preempts state “blue sky” registration requirements.

What it means: This is a potentially significant new exemption, but the requirements it imposes may result in sellers continuing to rely on existing exemptions and the Section 4(a)(1½) regime. It is possible, for instance, that the growing number of widely followed, privately-held companies, which have to date addressed demands for a resale market through repurchase programs, tender offers and a variety of private resale platforms, will welcome the express standards that this new Section 4(a)(7) provides in contrast to the uncodified Section 4(a)(1½). However, it is also possible that sellers may struggle to meet Section 4(a)(7)’s information and certification requirements with respect to non-reporting issuers. These challenges may not be as troublesome for resales of securities of a reporting company (for example, by investors purchasing in a PIPE offering) or of a foreign private issuer exempt from reporting pursuant to Rule 12g3-2(b) of the Exchange Act (for example, through a “block trade” on a foreign exchange), given that the seller would not be required to provide prescribed issuer information.

Another potential drawback of Section 4(a)(7) is that it may be difficult for sellers (and counsel delivering required transfer opinions) to become comfortable that no disqualifying “bad act” is present for any of the sale participants, especially in a fast-moving transaction. In this regard, it is notable that Section 4(a)(7), unlike Rule 506, **does not** provide an exception to “bad act” disqualification if the “bad act” could not have been discovered with reasonable care.

² Section 4(a)(7) also requires a seller to provide (i) the issuer’s name and address, (ii) the title, class and outstanding amount of the securities being sold and (iii) information regarding the issuer’s transfer agent.

Public Offerings by Emerging Growth Companies

The JOBS Act made capital raising through public offerings easier for a new category of issuer known as an emerging growth company (“EGC”), generally defined as an issuer with annual gross revenues of less than \$1 billion during its most recent fiscal year that was not already a public company as of December 8, 2011.³ The FAST Act enhances the framework created by the JOBS Act by providing additional flexibility to EGCs in initial and other public offerings in the areas described below.

1. Shortened IPO roadshow waiting period (*effective immediately*)

For EGCs, the FAST Act reduces the required waiting period between the initial public filing of an IPO registration statement and the start of the IPO roadshow from 21 days to 15 days.

What it means: During its IPO process, an EGC may submit a draft registration statement confidentially for the SEC’s review. Previously, EGCs were required to file their registration statement (as well as the initial confidentially submitted draft registration statement and all confidential amendments thereto) publicly with the SEC no later than 21 days before the EGC commenced its roadshow. As a result of the FAST Act, an EGC may now start the IPO roadshow closer in time to the public registration statement filing, which means that such companies will have additional flexibility to capitalize on favorable market conditions and thereby reduce execution risk.

2. Reduced financial statement burden (*effective immediately*)⁴

Prior to the Fast Act, an EGC was required to include in any registration statement two years of audited financial statements and unaudited financial statements covering any interim periods subsequent to the audited financials, regardless of whether those financial statements were expected to be required for inclusion in the registration statement at the time the public marketing effort began. The FAST Act provides that an EGC may omit in a registration statement financial information for historical periods otherwise required by Regulation S–X as of the time of filing (or confidential submission) of such registration statement, provided that (a) the omitted financial information relates to a historical period that the issuer reasonably believes will not be required to be included in the Form S-1 or F-1 at the time of the contemplated offering and (b) prior to the issuer distributing a preliminary prospectus to investors, such registration statement is amended to include all financial information required by Regulation S–X at the date of such amendment.

Example: An EGC issuer that is contemplating a December 2015 initial confidential submission and an April 2016 IPO launch could omit 2013 annual financial statements from the initial submission, since the 2013 annual financial statements would not be required at the time the IPO launches.

³ A company ceases to be an EGC upon the earliest to occur of the following events:

- its annual gross revenues exceed \$1 billion in a fiscal year;
- it has more than \$700 million in market value of its equity held by non-affiliates;
- it issues more than \$1 billion of non-convertible debt over a three-year period; or
- the end of the fiscal year following the fifth anniversary of its IPO.

⁴ While the FAST Act provides that EGC issuers could rely on this provision 30 days after enactment, the SEC’s Division of Corporation Finance has since issued guidance stating that it will not object if EGC issuers apply this provision immediately. See <http://www.sec.gov/corpfin/announcement/cf-announcement--fast-act.html>.

On December 10, 2015, the SEC issued guidance⁵ relevant to two important points not obvious from the text of the FAST Act:

- An EGC issuer **may not** omit interim financial statements from its filing or confidential submission relating to a period that will be included within required financial statements covering a longer interim or annual period at the time of the offering, even though the shorter interim period will not be presented separately at that time.

Example: In the scenario above, an issuer **could not exclude** its nine-month 2015 and 2014 interim financial statements from the initial confidential submission. The SEC's view in this case is that the 2015 and 2014 nine-month interim financial information "relates to" the annual financial information for 2015 and 2014 that will be included in the registration statement at the time of the launch of the April 2016 IPO, even though financial information for interim periods within 2014 and 2015 will not be separately presented in the preliminary prospectus.

- An EGC issuer **may** omit financial statements of other entities (for example, acquired businesses) from its filing or submission if it reasonably believes that those financial statements will not be required at the time of the offering.

Example: In the case of an EGC issuer that is contemplating a December 2015 initial confidential submission and an April 2016 IPO launch, the issuer may omit from the initial filing or confidential submission financial statements of an acquired business that would otherwise be required by Rule 3-05 of Regulation S-X if it expects that at the time of the April 2016 IPO the acquired business's financial results will have been reflected in the issuer's financial statements for a sufficient amount of time to obviate the need for separate financial statements.

What it means: This FAST Act provision will allow some EGC issuers to reduce costs and preparation time by excluding certain financial information that is not ultimately expected to be included in the registration statement at the time of the offering. However, EGCs will still have to prepare and have auditors review quarterly financial information that is required at the time of confidential submission, even when it is known at the outset that such quarterly financial information will not be separately presented in the registration statement at the time of the offering.

3. EGC treatment grace period provided (effective immediately)⁶

Under the FAST Act, if an issuer qualifies as an EGC at the time it initially submits or files an IPO registration statement but later in the IPO process ceases to qualify for such status, that issuer will continue to be treated as an EGC through the earlier of (a) its consummation of the IPO covered by the registration statement or (b) the one-year anniversary of the date it lost EGC status.

What it means: Previously, SEC interpretive guidance provided that if an issuer no longer qualified as an EGC during the course of the IPO process, it ceased being able to take advantage of the benefits of EGC status immediately.⁷ Under the FAST Act, issuers now generally have certainty

⁵ See <http://www.sec.gov/divisions/corpfin/guidance/fast-act-interps.htm>.

⁶ The SEC has also issued guidance stating that EGCs with registration statements pending at the time of enactment of the FAST Act may rely on this provision. See <http://www.sec.gov/corpfin/announcement/cf-announcement---fast-act.html>.

⁷ See the answer to question (3) of the SEC's Jumpstart Our Business Startups Act Frequently Asked Questions, available at: <http://www.sec.gov/divisions/corpfin/guidance/cfjobsactfaq-title-i-general.htm>.

about maintaining EGC treatment throughout the IPO process as long as the issuer qualified as an EGC at the time of the initial confidential submission.

Smaller Reporting Company Registration Statements (*SEC rulemaking required within 45 days of enactment*)

The FAST Act requires the SEC to amend Form S-1 to permit smaller reporting companies, as defined in Rule 405 under the Securities Act, to incorporate by reference any filings under the Exchange Act that they make after the effective date of a registration statement filed on Form S-1, referred to as “forward incorporation by reference.”

What it means: Currently, Form S-1 permits an issuer only to incorporate by reference disclosure in previously filed Exchange Act reports (“backwards incorporation by reference”). The FAST Act, however, now provides that a smaller reporting company may use forward incorporation by reference in a Form S-1 registration statement. This reduces the need for a smaller reporting company to update a Form S-1 resale⁸ registration statement by means of post-effective amendments, which can be time-consuming and are subject to SEC review. As a result of this change smaller reporting companies may be able to maintain resale shelf registration statements more conveniently and efficiently.

Simplifying Public Company Reporting Requirements

1. Form 10-K summary page (*SEC rulemaking required within 180 days of enactment*)

All reporting companies will be expressly permitted to submit a summary page in annual reports on Form 10-K as long as each item identified in the summary includes a cross-reference (which may be in the form of a hyperlink) to the corresponding material in its Form 10-K.

What it means: Currently, there is no requirement for companies to include summaries of disclosures contained in their Form 10-Ks, but at the same time, there is nothing which would prevent that. In this regard, summary disclosures are not specifically required in Securities Act registration forms but are standard features in prospectuses and are expected by investors and the SEC staff. Whether the permissive direction of the FAST Act and any subsequent SEC rulemaking will create a similar practice with the Form 10-K remains open. That said, the overall complexity and organizational structure of the Form 10-K and the resulting length and complexity of actual filings on that form certainly invite the use of a tool to help shareholders navigate the information being provided.

2. Revisions to Regulation S-K (*SEC rulemaking required within 180 days of enactment*)

The FAST Act requires rulemaking by the SEC to revise Regulation S-K to (a) further scale or eliminate disclosure requirements in order to ease the burden on EGCs, accelerated filers, smaller reporting companies and other smaller issuers and (b) eliminate provisions that are duplicative, outdated or otherwise unnecessary.

⁸ The text of the FAST Act does not limit forward incorporation by reference on Form S-1 for smaller reporting companies to resale registration statements. The form change required by the FAST Act, however, will not facilitate primary shelf offerings on Form S-1 for smaller reporting companies, because Rule 415, the rule which covers shelf offerings, only permits *primary* shelf offerings to be registered on Form S-3 or F-3.

The FAST Act also requires that the SEC conduct a study to determine how to modernize and simplify Regulation S-K by reducing the costs and burdens to reporting companies while continuing to provide all material information. In particular, the SEC is directed to emphasize a company-by-company approach that minimizes boilerplate language and evaluate methods of information delivery and presentation. Within 360 days of the enactment of the FAST Act, the SEC must provide a report of this study, including recommendations, to Congress, and is required to propose rules to implement its recommendations within 360 days of providing such report to Congress.

What it means: The SEC issued a report in 2013, mandated by the JOBS Act, containing the SEC staff's preliminary conclusions and recommendations about disclosure reform, and the staff of the SEC is currently embarked on a review of Regulation S-K and Regulation S-X as part of its disclosure effectiveness initiative.⁹ Further, the SEC and its staff have indicated a continuing focus on simplifying disclosure requirements with respect to small and emerging companies.¹⁰ These provisions of the FAST Act provide a firm timetable by which the SEC must unveil proposed revisions and provides particular areas of emphasis for such revisions.

If you have any questions concerning the material discussed in this client alert, please feel free to contact any of the following members of our Securities & Capital Markets practice group:

Bruce Bennett	+1 212 841 1060	bbennett@cov.com
Eric Blanchard	+1 212 841 1111	eblanchard@cov.com
Kerry Burke	+1 202 662 5297	kburke@cov.com
Warren Caywood	+1 212 841 1069	wcaywood@cov.com
David Engvall	+1 202 662 5307	dengvall@cov.com
Matt Franker	+1 202 662 5895	mfranker@cov.com
Matthew Gehl	+1 212 841 1113	mgehl@cov.com
Keir Gumbs	+1 202 662 5500	kgumbs@cov.com
D. Michael Lefever	+1 202 662 5276	mlefever@cov.com
David Martin	+1 202 662 5128	dmartin@cov.com
Donald Murray	+1 212 841 1101	dmurray@cov.com
Brian Rosenzweig	+1 212 841 1108	brosenzweig@cov.com
Kristian Wiggert	+44 20 7067 2280	kwiggert@cov.com

⁹ See <http://www.sec.gov/spotlight/disclosure-effectiveness.shtml>.

¹⁰ See, e.g., Commissioner Daniel M. Gallagher, "Opening Statement to the September 2015 Meeting of the SEC Advisory Committee on Small and Emerging Companies," September 23, 2015, available at: <http://www.sec.gov/news/statement/gallagher-advisory-committee-092315.html>.

Appendix A

Relevant FAST Act Sections

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