

# Securities Law Update: Companies Can Raise Capital by Advertising

THE JOBS ACT REMOVED A SIGNIFICANT BARRIER FOR COMPANIES SEEKING TO USE GENERAL ADVERTISEMENTS OR GENERAL SOLICITATIONS TO CONTACT INVESTORS AND RAISE CAPITAL. COMPANIES CAN NOW TAKE ADVANTAGE OF THIS RECENT CHANGE IN THE SECURITIES LAWS TO FUND THE NEXT STAGE IN THEIR GROWTH OR EXPANSION PLANS.

In order to successfully commence business operations, introduce new products or services, or expand into new markets, a company must be able to obtain adequate capital. There are numerous methods of obtaining capital, and a company's current stage of development and nature of business will dictate which transaction structure best fits the company's capital-raising needs.

Until recently, California companies generally could not use general advertising or solicitations to sell their securities unless the securities had been registered with the Securities and Exchange Commission (SEC) under its rigorous, extensive and expensive requirements in what is commonly known as a public offering.

Because of recent changes in the securities laws and related regulations of the SEC, however, companies may now use general advertising and solicitations to contact investors and sell company securities.

## **Background on Securities Regulation in the U.S.**

Shortly following the Great Depression, Congress enacted extensive laws regulating the offer and sale of securities in the United States. These laws are still largely in place today. Under these laws, any offer to sell securities must either be registered with the SEC or must be exempt from such registration requirements.

One such exemption specifically exempts "transactions by an issuer not involving any public offering," and the SEC adopted regulations to create certain safe harbors for complying with the private offering exemption (**Private Offering Regulations**). As a result, companies offering to sell securities are generally not required to formally register such offerings with the SEC if the offering meets the applicable requirements of the Private Offering Regulations.

Until the law was recently changed, however, one of the requirements of the Private Offering Regulations, with limited exceptions, was that the company could not use general advertising, or solicitations to offer, or sell its securities.

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## **Raising Capital Through Private Offerings**

Since their enactment in 1982, the Private Offering Regulations have provided a limited safe harbor for securities offerings in which the issuer (1) did not use general advertising or general solicitation, and (2) sold the securities to any number of accredited investors but not more than 35 non-accredited (but still sophisticated) investors.

While the Private Offering Regulations have historically served as one of the primary means for companies to raise capital, the prohibition on general advertising and general solicitation significantly limited companies' direct access to capital markets. On April 5, 2012, however, President Obama signed into law the Jumpstart Our Business Startups Act (**JOBS Act**), which was aimed at increasing American job creation and economic growth by improving access to the public capital markets.

As required by the JOBS Act, the SEC amended the Private Offering Regulations effective September 23, 2013, to, among other things, allow the use of general advertising and general solicitation to

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offer and sell securities provided that the following conditions are satisfied:

1. All purchasers of securities in the offering must be accredited investors (generally referring to natural persons having a net worth in excess of \$1 million or annual income in excess of \$200,000, or to business entities, employee benefit plans, trusts, or others persons meeting the criteria set forth in the federal securities laws), or the issuer reasonably believes that they are, at the time of the sale of the securities to that person;
2. The issuer takes reasonable steps to verify that all purchasers in the offering are accredited investors; and
3. Certain other provisions in the Private Offering Regulations are satisfied.

As a result, the JOBS Act has made it significantly easier for many companies, including companies in the grocery industry, to access public financing. Under the Private Offering Regulations, as revised, companies are now allowed to advertise their offerings on television, in newspapers and magazines, on the internet, in social media, and at seminars where attendees have been invited by general solicitation.

#### **Application to the Grocery Industry**

Due to its broad applicability, the Private Offering Regulations can now be used by start-up companies seeking initial capital from family and friends, by emerging companies seeking financing from angel investors or venture capital firms, and by established companies seeking additional capital from institutional investors.

Companies, including retailers, wholesalers, brokers, and suppliers in the grocery industry, should consider using the Private Offering Regulations to finance the next stage of their business development.

Private offerings can be significantly less costly than public offerings, and the JOBS Act has now made it significantly easier to contact the investors needed to obtain adequate funding.

#### **Words of Caution**

Although companies may now raise capital by using general advertising and solicitations under the Private Offering Regulations, as revised, other rules apply. Any company that offers and sells securities must ensure that there are no significant misstatements or omissions made to investors in connection with any offer or sale of securities.

For this reason, although not always required by the Private Offering Regulations, many companies provide potential investors with private placement memorandums or circulars (containing information such as company background and history, financial statements, and risk factors).

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In addition, investors are often times required to sign subscription agreements that include numerous representations and warranties about the investors to ensure that they are qualified investors. Also, federal and state securities filings are usually required when a company offers or sells securities.

It should also be noted that the federal and state securities laws are very complex, and the failure by a company to adhere to all applicable securities laws with regard to a securities offering can subject the company and management to significant civil and/or criminal liability. Prior to the commencement of any securities offering, it is highly recommended to seek the advice of experienced securities law counsel. ■

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