

## **Chapter 13**

### **SMALL PUBLIC OFFERINGS**

#### **INTRODUCTION**

Traditional public offerings are complicated, expensive and more likely to succeed when revenue approaches \$500 million. Few companies grow fast enough to attract venture capital. Banks cannot be relied on if a company is in an unusual or disfavored industry or if it has limited collateral and Angel investors invest small amounts. Federal and state regulations restrict sales of securities issued in private placements and without the ability to resell shares, investments become unattractive.

Small public offerings overcome most of these problems for companies with the right profile. The ideal company for a small public offering has a history of profits, is growing, but not fast enough to attract venture capital, has a product that is easy to understand and brand recognition. The two main issues that differentiate small public offerings from a traditional IPO are: (i) simplified regulation and (ii) the means of distributing stock to the public.

#### **REGULATION OF SMALL PUBLIC OFFERINGS**

Federal securities law provides three regulatory options for a small public offering: (i) Regulation A, Form 1-A; (ii) Form SB-1; and (iii) Form SB-2. Each must comply with state as well as federal law. Generally, the more money a company raises, the more complex the regulation.

## Regulation A Registration

Regulation A is an SEC regulation allowing companies to raise up to \$5 million in one year. Regulation A permits limited advertising, does not restrict who the securities may be sold to, or the number of investors, and allows stock to be resold in the secondary market. An important feature of Regulation A is a provision to “test the waters.”

“Testing the waters” is a unique feature of Regulation A in that it allows a company to determine whether there is any interest in an offering before making it effective. In essence, a company can advertise, within limits, and have people respond with an expression of interest in the stock in the form of a subscription or coupon. The details of this testing provision are set forth in Regulation A, for example:<sup>1</sup>

- (i) An issuer may publish or deliver to prospective purchasers a written document or make scripted radio or television broadcasts to determine whether there is any interest in a contemplated securities offering.
- (ii) The text of the solicitation or script of the broadcast must be filed with the SEC (Attention: Office of Small Business Review) prior to its dissemination.
- (iii) Communications are subject to statutory anti-fraud provisions.
- (iv) No solicitation or commitment from any prospective investor is permitted until qualification of the offering statement.
- (v) The written document or script of the broadcast shall state that (a) no money or other consideration is being solicited; (b) no sales will be made or commitment to purchase accepted until delivery of an offering circular; (c) an indication of interest made by a prospective investor involves no obligation or commitment of any kind; and (d) the identity of the chief executive officer and briefly describe the company and its products.
- (v) Solicitations of interest pursuant to this provision may not be made after the filing of an offering statement.