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Comment

The JOBS Act: Effects on Capital Market Competition in Both Public and Private Markets

Tom Wentzell*

Introduction

Nothing has shaped modern culture in the twenty-first century quite like Facebook, so much so that the influence has even spilled over to the federal securities laws. In 2012, Facebook became a public company, generating sixteen billion dollars through an initial public offering (IPO) of its shares.[1] Though now publically owned, much has been made of a sequence of events that allowed Facebook to remain a private company for a significant period of time before its IPO. In late 2010, Goldman Sachs proposed to sell a large number of Facebook shares to various investors.[2] Had the sale gone through, Facebook stock arguably would have been held by enough shareholders that Facebook would have been required to register as a public company under the US securities laws.[3] With Facebook not wanting to be exposed to registration requirements under the US securities laws, Goldman Sachs brought the transaction outside of the United States.[4] To some members of the public, and indeed to opportunistic lawmakers, the off-shoring of this transaction marked a failure of the American economic system's ability to stimulate, or even allow for, capital formation.[5] American lawmakers who had so recently witnessed a beefing up of regulatory oversight through the Sarbanes-Oxley Act and the Dodd-Frank Act, capitalized on the oppor-

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1. Lee Spears & Sarah Frier, *Facebook Stalls in Public Debut After Record $16B in IPO*, Bloomberg (May 18, 2012, 5:55 PM), http://www.bloomberg.com/news/2012-05-17/facebook-raises-16-billion-in-biggest-technology-ipo-on-record.html.

2. Adam C. Pritchard, *Revisiting "Truth in Securities" Revisited: Abolishing IPOs and Harnessing Private Markets in the Public Good*, 36 Seattle U. L. Rev. 999, 1006 (2013).

3. *Id.*

4. *Id.*

5. *Id.* at 1008.

tunity to criticize the Securities Exchange Commission (SEC) and push for legislation that was deregulatory and more "pro-growth" in nature.[6]

Critics saw the off-shore Facebook transactions as representative of a broader trend, in which the United States has gradually become less dominant in its position as the most powerful capital-raising venue in the world. Over the course of the last twenty years, United States capital markets have indeed become relatively less competitive, across a variety of metrics. When the comparison period is narrowed to only the last ten years, it is even more evident that the United States is not the singular, capital-raising powerhouse that it was in the last decade of the twentieth century.[7] Certainly, there is a debate as to how much this status matters. If issuers of securities are attracted to a country's capital raising environment, but that environment is deregulated to such an extent that investors are not adequately protected, it is not necessarily a weakness to be "less competitive." Investor protection concerns notwithstanding, the trend of fewer foreign companies bringing their transactions to the United States has not been lost on lawmakers.

In April of 2012, Congress passed and President Obama signed the Jumpstart Our Business Startups Act (hereinafter the "JOBS Act" or the "Act"), in an effort to improve the competitive position of US capital markets.[8] This paper examines certain changes called for by the JOBS Act, and provides analysis as to whether these changes are likely to improve the competitive position of US capital markets. The paper looks at those portions of the JOBS Act that were effective immediately upon its passage, examines related SEC rulemaking on general solicitation and general advertising, and predicts whether the changes established by the JOBS Act will in fact jumpstart capital formation for early stage companies.

Part I offers a snapshot of the current state of US capital market competitiveness, focusing primarily on data compiled in the last twenty years by the Committee on Capital Markets Regulation (CCMR). This snapshot of US markets shows that private capital markets are burgeoning, but public markets are stagnating—or even regressing—compared to other countries. Part II highlights policy makers' responses to the declining competitiveness of US markets. Their responses exhibit awareness among policy makers that the depth and liquidity of capital markets has a direct impact on early-stage companies' ability to attract investment and grow their businesses. Such investment allows companies to grow and create jobs, which is currently a primary concern of lawmakers. Part III offers a description of the JOBS Act, with a particular emphasis on Titles I, II, and V of the Act. Part III goes on to analyze the JOBS Act through the specter of whether or not it

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6. *See id.* (stating that "Goldman's failed private offering of Facebook shares triggered a rather dramatic legislative response").

7. *See infra* Section I.

8. *See infra* note 34 and accompanying text.

is likely to cure any of the deficiencies present in US capital markets, and what tertiary effects the Act might have as a result of its emphasis on capital formation.

This paper—for the most part—does not discuss investor protection issues relevant to the JOBS Act, though the debates on that topic are numerous and provocative. Unlike Sarbanes-Oxley or Dodd-Frank, the primary focus of the JOBS Act is not investor protection. As outlined below, the JOBS Act focuses on capital formation, and this paper will primarily analyze how effective the Act is in promoting that objective. Taking a comprehensive view of the JOBS Act, it should moderately improve the attractiveness of US capital markets overall, but the net benefit to public markets and the initial public offering market, in particular, is likely to be negligible, if not nil.

I. The Competitive Position of US Capital Markets

Various theories attempt to explain the trend of decreasing competitiveness in the US capital markets, some of which point directly to the structures of the US financial system, and others that do not. One scholar, Stephen Bainbridge from the University of California–Los Angeles, argues that corporate governance reforms under the Sarbanes-Oxley Act and Dodd-Frank Act have made operating as a public company in the United States less appealing.[9] Bainbridge asserts that both the primary and secondary public markets have suffered in the wake of the "federalizing" of corporate governance.[10] Notwithstanding Bainbridge's views on causation factors, his assertion that primary markets (*i.e.*, initial public offerings) and secondary markets (*i.e.*, the resale markets) are struggling is borne out by the data provided below.[11] This illustrates how the expenses that deter companies from going public in the United States are not only those expenses related to conducting an IPO, but also those from the continuing reporting obligations attendant to public company status. Bainbridge argues that it is not so much the principles of the regulatory rules that are a burden to American public companies, but rather the "sheer volume of regulations with which issuers must comply."[12]

Another scholar, John C. Coffee, Jr., of Columbia University, notes that the litigation environment in the United States is "likely to discourage the foreign issuer from entering the U.S. market."[13] Coffee refers to this as

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9. *See* Stephen M. Bainbridge, Corporate Governance After the Financial Crisis 261–68 (2012) (describing the "federalizing" of corporate governance law through Sarbanes-Oxley and Dodd-Frank, which has added significant regulatory compliance costs for public companies).

10. *Id.* at 261–62.

11. *See infra* notes 17–30 and accompanying text.

12. Bainbridge, *supra* note 9, at 264–65.

13. John C. Coffee, Jr., *Law and the Market: The Impact of Enforcement*, 156 U. Pa. L. Rev. 229, 302 (2007).

"private enforcement" in the securities market, and suggests that it makes a foreign firm less likely to cross-list its shares on a US exchange because doing so exposes it to potentially global class action lawsuits.[14]

Foreign developments, however, are also partly responsible for the relative decrease in the competitiveness of the US capital markets. As foreign jurisdictions have improved their regulatory policies and legal institutions, they have encouraged growth in their own markets.[15] If a foreign market improves its capital supply, a foreign firm has a lesser need to come to the United States to raise capital. Though such growth could be a positive for the overall health of the US economy,[16] it also lessens America's dominance over, and relative competitive position within, capital markets. Either way—whether US markets are fundamentally flawed or foreign countries are more effectively positioning their capital markets than in previous years—the data show that US capital markets are relatively weaker than they were before the turn of the century.

Much of the most useful research illustrating the changing landscape of capital market competition comes from the Committee on Capital Markets Regulation (CCMR), an independent, non-partisan research organization that studies the regulation of US capital markets.[17] CCMR maintains an updated collection of data that tracks various metrics that serve as indicators of capital market competitiveness. These measures in their entirety paint a picture of a US financial system that was at its most competitive in the mid- to late-1990s, but has gradually ceded its dominance starting in the first decade of the twenty-first century.[18]

For example, in the year 2000, American stock exchanges accounted for 63.9% of the total value of share trading worldwide, with respect to trading on exchanges that are members of the World Federation of Exchanges.[19] This figure has since dropped steadily, and in 2012, it stood at 47.5%.[20] The data also show that between 2002 and 2012, the average annual growth in the gross value of share trading increased by 5.3% on foreign exchanges, but only 2.3% on US exchanges.[21] So even though the

14. *Id.* at 302–03.

15. Michael J. Ryan Jr., CTR. FOR CAPITAL MKTS. COMPETITIVENESS, U.S. CAPITAL MARKETS COMPETITIVENESS: THE UNFINISHED AGENDA 31 (2011), *available at* https://www.uschamber.com/sites/default/files/reports/1107_UnfinishedAgenda_WEB.pdf.

16. *See id.* (explaining that successful foreign markets can bolster the U.S. market by supplying a wider range of goods and services and a lower cost of capital).

17. COMM. ON CAPITAL MKTS REGULATION, http://capmktsreg.org (last visited June 6, 2013).

18. *See generally Competitiveness Measures*, COMM. ON CAPITAL MKTS. REGULATION, http://capmktsreg.org/education-research/competitiveness-measures/ (last visited, June 6, 2013).

19. *Measure 11 – U.S. Share of the Value of Global Share Trading*, COMM. ON CAPITAL MKTS. REGULATION, http://capmktsreg.org/wp-content/uploads/2013/02/11Value_of_Share_Trading_on_Member_Exchanges_of_the_World_Federation_of_Exchanges_12_4.pdf (last visited June 6, 2013) (attached to this article as Appendix A).

20. *Id.*

21. *Id.*

global financial crisis was—as inferred by its common parlance—a blow to financial systems worldwide, these data show in a comparative fashion that US public markets were more severely set back and have rebounded less rapidly than foreign public markets.

Another indicator of decreasing competitiveness in the United States is that its relative share of Global Initial Public Offering ("Global IPOs") activity has decreased significantly.[22] "Global IPOs" are defined as "IPOs by foreign companies outside their home countries."[23] Between 1996 and 2000, the total number of Global IPOs that were captured by US exchanges in a given year ranged between 46.4% and 58.1%.[24] Since then—though the decline in activity has not been linear—the percentage of Global IPOs captured by US exchanges since 2001 has ranged between 6.4% and 26.1%.[25] With respect to Global IPO activity in terms of total dollar value, America's drop has not been quite as precipitous, although it still has been significant.[26] The lesser decrease, measured in dollar value, indicates that among the Global IPOs that US markets are still able to attract, a disproportionate number are large offerings. Global IPOs as a whole, however, are coming to the United States at a less frequent rate. The fact that smaller companies are faring proportionately worse than larger companies in this category underscores the importance of the JOBS Act's emphasis on small and emerging companies.

Finally, to the extent that foreign issuers are raising capital in the United States, they are doing so more frequently through private markets. According to the CCMR, the amount of equity raised by foreign issuers through private Rule 144A American Depository Receipt (ADR) offerings, taken as a percentage of the amount of capital raised by foreign issuers in public equity markets, has increased over the last eight years.[27] From 2000 to 2004, Rule 144A offerings ranged between 1.0% and 3.5% of the amount of equity raised through public markets.[28] From 2005 to 2012, this number ranged between 3.8% and 46.8%, and in four of those eight years the percentage was in the double-digits.[29] Although Rule 144A offerings comprise

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22. *See generally Equity Raised in Public Markets*, COMM. ON CAPITAL MKTS. REGULATION, http://capmktsreg.org/wp-content/uploads/2013/02/2Share_of_Global_IPO_12_4_1-of-2.pdf (last visited June 6, 2013) (defining various measures used to examine performance in capital markets).

23. *Id.*

24. *Measure 2 – Global IPOs by Foreign Companies (Narrowly Defined)*, COMM. ON CAPITAL MKTS. REGULATION, http://capmktsreg.org/wp-content/uploads/2013/02/2Share_of_Global_IPO_12_4_1-of-2.pdf (last visited June 6, 2013) (attached to this article as Appendix B).

25. *Id.*

26. *See id.*

27. *Measure 7 – Relative Size of the Private Rule 144A and Public Equity Markets*, COMM. ON CAPITAL MKTS. REGULATION, http://capmktsreg.org/wp-content/uploads/2013/02/7Equity_Raised_by_Foreign_Issuers_Via_Rule_144A_12_4.pdf (last visited June 6, 2013) (attached to this article as Appendix C).

28. *See id.*

29. *See id.*

only part of the private market, they are an alternative that many foreign companies use to avoid listing in the United States, and these data show that the Rule is increasingly being used. Also, the increasing ratios described in this paragraph are the result of both increased participation in the Rule 144A private market and flat or *decreased* participation in public equity markets.[30] Thus, the data show more than simply a burgeoning of the private equity markets; rather, they truly reflect a weakening of US public equity markets.

II. The JOBS Act Responds to Weaknesses in US Capital Markets

The decreasing competitiveness of US public capital markets has not been lost on American policy makers. On December 8, 2011, Representative Stephen Fincher from Tennessee introduced what would later become the JOBS Act.[31] In his brief opening remarks, Representative Fincher described the decrease in US IPO activity, and how this is of concern to the US economy because "over 90 percent of job growth occurs after a company goes public."[32] He called American regulation of capital markets a "one-size-fits-all" approach and showed concern that such regulations imposed a "disproportionate cost" on smaller companies, thus making it less desirable to become public and more onerous for those who already are public.[33] The focus of Representative Fincher's concerns was clearly on public markets.

The introductory text of the JOBS Act itself imbues a public market emphasis. The Act states as its purpose: "To increase American job creation and economic growth by *improving access to the public capital markets* for emerging growth companies."[34] Similarly, the captions of each Title give rise to an unmistakable inference of the pro capital formation policy legislators sought to achieve through the JOBS Act. For example: "Title I—Reopening American Capital Markets to Emerging Growth Companies," "Title II—Access to Capital for Job Creators," and "Title V—Private Company Flexibility and Growth."[35] This legislation was put forth to spur capital markets, and notably, it passed with widespread bipartisan support.[36]

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30. *See id.*

31. 157 Cong. Rec. E2210 (daily ed. Dec. 8, 2011) (statement of Rep. Stephen Fincher).

32. *Id.*

33. *Id.* at E2210–11.

34. Jumpstart Our Business Startups (JOBS) Act, Pub. L. No. 112-106, 126 Stat. 306 (2012) [hereinafter "JOBS Act"] (emphasis added).

35. *Id.*

36. Seung Min Kim, *JOBS Act Passes Congress, Heads to Obama*, Politico (Mar. 27, 2012, 7:19 PM), http://www.politico.com/news/stories/0312/74539.html (noting passage in the House by a margin of 380 to 41, and passage in the Senate by a margin of 73 to 26).

Representative John Carney was another chief author of the JOBS Act.[37] Representative Carney urged his colleagues to pass the legislation because it would make it easier and less costly for companies to go public.[38] He emphasized that the JOBS Act would not grant exemptions for companies seeking to go public, but rather, it allowed for "phasing in [of] certain costly regulatory requirements."[39] Though he acknowledged that there was much debate surrounding certain provisions of the bill, he noted that the Financial Services Committee passed the bill with a bipartisan vote of fifty-four to one.[40]

Even since the passage of the JOBS Act, legislators have reiterated the importance of the Act's policies as it goes through the process of rulemaking before the Securities Exchange Commission (SEC). In a letter to then-SEC Chairman Mary Schapiro regarding implementation of Title II of the Act, Representative Patrick McHenry referred to the JOBS Act as "critical reform."[41] McHenry, Chairman of the Subcommittee on TARP, Financial Services and Bailouts of Public and Private Programs, was dismayed at Chairman Schapiro's alleged foot-dragging in putting forth SEC rules, and complained that the SEC's delay was a "significant obstacle to capital formation and economic recovery."[42]

Certainly the JOBS Act is not without its opponents—particularly those concerned with investor protection issues related to Title II—but this paper considers the legislation for its effectiveness in achieving the objectives sought by its proponents and the purpose articulated in its text.[43] The following section explores how the JOBS Act is likely to impact the competitive position of US capital markets, predicting what its effects will be on both public and private markets. The paper will only examine Titles I, II, and V of the Act. Title III is the "crowdfunding" exemption which is not yet effective and will require extensive SEC rule-making.[44] Title IV allows companies to issue to the public, under Regulation A, up to $50 million in equity, debt, or convertible securities in a year without having to register, but it also is not addressed in this paper as it too relies on SEC rulemaking

37. *Full Biography*, U.S. CONGRESSMAN JOHN CARNEY, http://johncarney.house.gov/index.php?option=com_content&view=article&id=18&Itemid=7 (last visited Feb. 6, 2013); *see* 158 CONG. REC. H1236–37 (daily ed. Mar. 7, 2012) (statement of Rep. Spencer Bachus).

38. 158 CONG. REC. H1237–38 (daily ed. Mar. 7, 2012) (statement of Rep. John Carney).

39. *Id.* at H1238.

40. *Id.*

41. Letter from Patrick McHenry, Chairman of the Subcommittee on TARP, Financial Services and Bailouts of Public and Private Programs, to Mary Schapiro, SEC Chairman (Nov. 30, 2012), *available at* http://www.sec.gov/comments/s7-07-12/s70712.shtml.

42. *Id.*

43. *See* JOBS Act, *supra* note 34.

44. *See id.* at § 302; *see also Information Regarding the Use of the Crowdfunding Exemption in the JOBS Act*, SEC. AND EXCH. COMM'N (Apr. 23, 2012), http://sec.gov/spotlight/jobsact/crowdfundingexemption.htm ("reminding" issuers that any crowd-funding before the implementation of SEC rules is unlawful under the securities laws).

that has yet to begin as of the summer of 2013.[45] Title VI is not discussed because it relates only to community banks and not to issuers of securities generally, and Title VII is omitted from this discussion because it is merely an education and outreach mandate to the SEC.[46]

III. Analyzing the Effectiveness of the JOBS Act in Improving US Capital Market Competitiveness

Although the JOBS Act contains certain elements that are keenly targeted to achieve various (though sometimes competing) objectives, the Act taken as a whole does not significantly further the goal of making US capital markets more attractive to foreign companies deciding where to list their shares. In particular, the Act's effect on public markets is minimal, as the greatest improvements from the standpoint of attracting capital will be in the private markets. Improvements to the IPO process are largely offset by a company's ability to access new sources of capital while still remaining private. Thus, though the IPO process has improved, the incentive has to go public have also decreased.

A. *Title I: Reopening American Capital Markets to Emerging Growth Companies*

Title I, or the "IPO on-ramp," was enacted with the purpose of making it less burdensome for a smaller issuer to conduct an initial public offering (IPO), and less burdensome for a smaller issuer to operate as a public company in the early years after its IPO.[47] Title I created a class of issuers called "Emerging Growth Companies," (EGCs) which are companies that have less than $1 billion in annual revenue and less than $700 million in worldwide market value of equity securities—otherwise known as a company's public float.[48] A company retains EGC status for as long as it stays below the thresholds for annual revenue and public float, or until the final day of the fiscal year following the fifth anniversary of its IPO.[49] The other key defining feature of an EGC is that an issuer is only eligible for EGC status if its first public sale of securities came after December 8, 2011.[50]

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45. *See* JOBS Act, *supra* note 34, at § 401; *see also* Bob Kaplan & Tom Voekler, *Beyond Crowdfunding: Why Regulation A Reform is the most Vital Piece of the JOBS Act*, The Wash. Post (June 13, 2012), http://articles.washingtonpost.com/2012-06-13/business/35459353_1_initial-public-offerings-investors-jobs-act (describing the basic operation of Regulation A).

46. *See* JOBS Act, *supra* note 34, at §§ 601, 701.

47. *See, e.g.*, Latham & Watkins Capital Markets Group, *Client Alert No. 1308: JOBS Act Establishes IPO On-Ramp*, Latham & Watkins (Mar. 27, 2012), http://www.lw.com/upload/pubContent/_pdf/pub4711_1.pdf.

48. JOBS Act, *supra* note 34, at § 101; *see also* Securities Exchange Commission, 17 C.F.R. § 240.12b-2 (2012) (defining worldwide market value requirements for issuers).

49. *See* JOBS Act, *supra* note 34, at §§ 101(a), (b).

50. *Id.* at § 101(d).

Under Title I, the JOBS Act confers numerous benefits on EGCs. Some of these benefits relate to corporate governance and audits—benefits an EGC will enjoy *after* it has already become public. A summary of those post-IPO benefits is as follows:

- EGCs are not required to hold votes on executive compensation ("Say-on-Pay") or on executive golden parachute compensation.[51]
- EGCs going public for the first time need only two years of audited financial statements instead of the three years that is normally required.[52]
- EGCs are not required to adhere to any auditor rotation rules established under the Sarbanes-Oxley Act or by the Public Company Accounting Oversight Board.[53]
- When public companies file annual reports, they are required to include an "internal control report," which is a description and an assessment of the effectiveness of their control structures related to financial reporting.[54] Under section 404 of Sarbanes-Oxley, the accounting firm that issues this report must "attest to, and report on" the assessments made by the management of the issuer. The JOBS Act, however, removes auditor attestation requirement for EGCs.[55]

With Title I, the JOBS Act created what some might consider an intermediate status that is more demanding than private company status, but does not impose the full rigor of the normal public company reporting regime. The benefits conferred by Title I are ongoing for as long as a company retains Emerging Growth Company status—either until after the five-year anniversary of the company's IPO or until it becomes too large, based on annual revenue and public float.[56]

Other benefits that EGCs enjoy are specifically related to the initial public offering of their securities. These benefits include:

- Broker-dealers are allowed to publish research reports regarding EGCs even if the broker-dealer is participating in that EGC's public offering. Importantly, these reports will not be considered offers under the securities laws.[57]
- Various communications by research analysts are explicitly permitted, thereby deconstructing the wall between analysts

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51. THE LIBRARY OF CONGRESS, JUMPSTART OUR BUSINESS STARTUPS: BILL SUMMARY AND STATUS (Apr. 5, 2012), http://thomas.loc.gov/cgi-bin/bdquery/z?d112:HR03606:@@@L&summ2=m&.

52. *See* JOBS Act, *supra* note 34, at § 102(b).

53. *Id.* at § 104.

54. Sarbanes-Oxley Act § 404, 15 U.S.C. § 7262 (2012).

55. *See id.*; *see also* JOBS Act, *supra* note 34, at § 103.

56. *See* JOBS Act, *supra* note 34, at §§ 101(a)–(b).

57. *Id.* at § 105(a).

and other parties involved in the offering—particularly investment bankers.[58]

- EGCs are allowed to submit a draft version of their registration statements to the SEC for confidential review.[59]

Additionally, the SEC has indicated that foreign private issuers will be treated the same under the JOBS Act as domestic issuers, even though the plain language of the text of the JOBS Act confers on issuers benefits that are specific to domestic filings.[60]

Given the relief described above, Title I of the JOBS Act should have some positive impact in stimulating IPO activity in the United States, as it creates an attractive status that companies can enjoy for roughly five years. The issue remains, though, as to whether that impact will be significant enough to stem the tide of decreasing IPO activity in the United States.

At the time this paper was drafted, a small sample of data was available regarding IPO activity since the passage of the JOBS Act. These studies admit that they are unable to isolate the extent to which IPO activity has been driven by the JOBS Act, but they do provide an initial glimpse after one year of the JOBS Act. On the whole, IPO activity in the first year after the Act's passage was slightly up from the prior year.[61] Additionally, eighty-three percent of the companies that conducted an IPO in the first year of the JOBS Act were EGCs.[62] The fact that companies are using the EGC status, however, does not necessarily mean that the availability of such a status is what is pushing them into the IPO market. In fact, the amount of companies going public in 2012 that had annual revenues under $1 billion (the revenue limit for EGCs) was 113, while in 2011 that same number was 114.[63] Thus, while companies are taking advantage of EGC status, and commentators are finding that EGC status may have "meaningfully improved and reduced the cost of the IPO process," it is unclear what effect these provisions are having in driving the number of IPOs.[64]

On June 8, 2012, shortly after the passage of the JOBS Act, at a meeting of the Advisory Committee on Small and Emerging Companies, Jen-

58. *Id.* at §§ 105(b)–(d).

59. *Id.* at § 106(a).

60. *See Generally Applicable Questions on Title I of the JOBS Act*, SECURITIES EXCHANGE COMMISSION, quests. 8–10 (Apr. 16, 2012), http://www.sec.gov/divisions/corpfin/guidance/cfjjobsactfaq-title-i-general.htm (stating that if a foreign issuer qualifies for EGC status and chooses to take advantage of the benefits EGCs are entitled to, the SEC will not object to the issuer complying with the same disclosure provisions as domestic EGCs, even though some of the reporting forms differ).

61. Martin Wellington & Sarah Solum, *On its One-Year Anniversary, Two Cheers for the JOBS Act*, FORBES (Mar. 28, 2013) http://www.forbes.com/sites/realspin/2013/03/28/on-its-one-year-anniversary-two-cheers-for-the-jobs-act/; ERNST & YOUNG, THE JOBS ACT: ONE-YEAR ANNIVERSARY 3 (2013), *available at* http://www.ey.com/Publication/vwLUAssets/The_JOBS_Act:_One-year_anniversary/$FILE/JOBSActAnniversary_CC0368_9April2013.pdf.

62. ERNST & YOUNG, *supra* note 61, at 4.

63. *Id.* at 3.

64. Wellington & Solum, *supra* note 61.

nifer Zepralka of the SEC stated that the Commission had received "about 30" confidential submissions of draft registration statements in the initial two months after the bill was signed.[65] It was a hopeful piece of anecdotal data, indicating that issuers were at least showing interest in the draft registration statement provisions.

A separate contributor to the Advisory Committee on Small and Emerging Companies had a less enthusiastic, though not negative, review of Title I of the JOBS Act. Gregory Yadley is a Florida securities attorney who said that as of the meeting on June 8, 2012, he had not seen a great difference in the level of interest in conducting an IPO.[66] He explained "[t]his is not a negative reaction. I think it's just, wow, there's a lot going on, it's pretty complicated. What's really different?"[67]

Mr. Yadley's sentiment has been echoed in the initial scholarly reviews of the JOBS Act. Zachary Gubler of Arizona State University claims that the public securities market in the United States has been and continues to be "dysfunctional."[68] Gubler called the JOBS Act "puzzling," in that its "deregulatory agenda" did not focus so much on reforming public markets—perhaps through rolling back a greater portion of the Sarbanes-Oxley Act—but instead on deregulating private markets.[69] Reflecting his conclusion that the JOBS Act did not mark any significant improvement to the IPO market, Gubler states the following:

> The dysfunctional IPO market creates pressure to either reform the public market or expand the private one. Just as the SEC has done for the past decade, Congress decided to expand the private securities market with the JOBS Act because this alternative offers greater political slack and avoids the uncertainty that accompanies any attempt at diagnosing and solving the underlying problem with the public market.[70]

Gubler clearly thinks that the public market received no help from the JOBS Act.

In regards to the EGC provisions of Title I of the JOBS Act, Adam Pritchard of the University of Michigan Law School asserts that "these provisions of the JOBS Act are far from revolutionary."[71] Shortly after the passage of the JOBS Act, Pritchard advocated giving issuers more choice

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65. U.S. Securities and Exchange Commission Transcript of Fourth Meeting of Advisory Committee on Small and Emerging Companies 6 (June 8, 2012), *available at* http://www.sec.gov/info/smallbus/acsec/acsec060812-transcript.pdf [hereinafter Advisory Committee Meeting].

66. *See id.*; *See also Gregory C. Yadley,* SHUMAKER, LOOP & KENDRICK, LLP, http://www.slk-law.com/Lawyers/Gregory-C-Yadley (last visited Sept. 15, 2013) (describing biographic information and work experience for Gregory C. Yadley).

67. Advisory Committee Meeting, *supra* note 65, at 9.

68. Zachary J. Gubler, *Public Choice Theory and the Private Securities Market*, 91 N.C. L. REV. 745, 796 (2013).

69. *Id.* at 795.

70. *Id.* at 796.

71. Pritchard, *supra* note 2, at 1011.

over whether to operate as a private or public company.[72] Under his scheme, issuers would be *eligible* for public company status based on certain quantitative benchmarks, but the decision to go public would be voluntary and rest with the issuer.[73] Though Pritchard's paper chiefly outlined his proposed alternative reporting regime, he commented briefly on the JOBS Act saying that although it "pushed back" some of the qualifying lines that require a company to comply with public company status, overall it "fail[ed] to address the fundamental inefficiency of the market for IPOs."[74]

While I am intrigued by Pritchard's proposal to make the reporting regime semi-elective, my own conclusion regarding Title I of the JOBS Act is that it could have been far more effective even without the fundamental changes suggested by Pritchard. With just a few minor tweaks from the final form of the bill, the Act could have been far more effective in generating IPO activity than it is projected by many to be. First, the Title I should not have limited a company's ability to enjoy EGC status to only five years.[75] This creates uncertainty for an issuer considering whether to go public because the issuer has to consider significant and uncertain reporting requirements it will face five years down the road, even if its business has not grown quickly enough to absorb the associated costs of such reporting. Second, Title I should have given relief to issuers that went public before December 8, 2011.[76] Excluding such companies from EGC status shrinks the pool of eligible issuers that could enjoy less stringent reporting requirements, and with that, enjoy greater flexibility to spur growth.

Title I of the JOBS Act in effect created an intermediate status between public companies and private companies when it created the Emerging Growth Company definition. In this sense, it attempted to veer away from the "one-size-fits-all" approach criticized by Representative Fincher.[77] While it is debatable whether the size of a company's shareholder roster is a relevant factor for determining whether a company should be considered "public,"[78] the EGC status did indeed attempt to provide relief and flexibility to smaller companies, which was one of the legislative concerns discussed above.[79] However, while companies qualify for EGC status based on size, they may nonetheless be disqualified from this status based on the duration of time for which they are an EGC. This creates incongruence in

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72. Adam C. Pritchard, *Facebook, the JOBS Act, and Abolishing IPOs*, REGULATION, Fall 2012, at 12, 15–17, *available at* http://www.cato.org/sites/cato.org/files/serials/files/regulation/2012/11/v35n3-3.pdf.

73. *Id.* at 15–16.

74. *Id.* at 15.

75. *See* JOBS Act, *supra* note 34, at §§ 101(a)–(b).

76. *Id.* at § 101(d).

77. *See* 157 CONG. REC. *supra* note 31, at E2210–11.

78. *See* Donald C. Langevoort & Robert B. Thompson, *"Publicness" in Contemporary Securities Regulation After the JOBS Act*, 101 GEO. L.J. 337, 340–41 (2013) (arguing that a company's trading volume is a more appropriate metric for determining "publicness").

79. *See supra* notes 32–34 and accompanying text.

the criteria that an issuer has to consider in determining whether or not to conduct an IPO. Thus, while an EGC incurs lower expenses connected to the initial public offering of its securities and fewer expenses in complying with subsequent disclosure requirements once public, it is guaranteed to face a more expensive reporting regime five years down the road, regardless of its size at the time. Companies making the decision to go public are thus not only forced to look at current revenues and revenue projections for the near future, but they must also project revenue for years six and beyond, and forecast that against a more expensive reporting regime.

One such expense is the previously discussed internal controls reports of Sarbanes-Oxley Section 404. Bainbridge reports that to become compliant with Section 404, large firms spent an average of $7.3 million in year one, while smaller public firms spent an average of $1.6 million in year one.[80] Thus, an EGC deciding to go public must account for the expense of the internal controls, not knowing exactly when they will incur the expense, how expensive it will be, or whether the company will have the revenues to afford that expense while continuing to grow its business. If the EGC status were based solely on size, an issuer would only be exposed to the expense of the internal controls report once it was correspondingly bringing in a larger amount of revenue (or whatever other quantitative benchmark is established to define a company as "public"). Such a regime would give issuers greater certainty and predictability as they strategize as to how they will raise capital. Whether it is a foreign firm considering US markets or a US company contemplating when to go public, certainty and predictability of cost will make that issuer more likely to choose the US IPO market as its next capital raising venue.

The second simple, but significant, failure I see in Title I is that EGC status is only available to issuers who go public after December 8, 2011. Thus, a small public company's ability to grow, absent the burdens and expenses previously discussed, arbitrarily depends on when it first chose to go public.[81] Admittedly, the emphasis of Title I is to encourage IPO activity, and companies who went public before the introduction of this Act are not likely to be conducting an IPO again anytime soon,[82] but the ongoing benefits to EGCs are still noteworthy and could have been beneficial to other smaller issuers. Opening up EGC status to issuers who went public before December 8, 2011, would not only satisfy notions of fairness, but it would also reduce regulatory compliance costs for small companies, thereby increasing profits and giving them opportunities to grow their businesses and their workforces.

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80. Bainbridge, *supra* note 9, at 8–9.

81. *See supra* text accompanying notes 42–46.

82. The exception to this is that, if a company is able, it could cause itself to become private, only to later use the EGC status to go public again through an IPO.

There are attractive benefits attendant to Emerging Growth Company status, but similar to Pritchard and Gubler, I do not see Title I as creating a fundamental change that will encourage more frequent IPO activity in the United States. While the benefits to EGC status are noteworthy, the road-blocks to attaining and/or retaining that status will likely stifle the potential effectiveness of Title I.

B. Title II: Access to Capital for Job Creators

If Title I was the political rallying point that largely unified lawmakers behind the cause of jump-starting IPO activity, the private offering reforms under Title II caused a political firestorm that has drawn spirited input from investor advocates, business interests, the SEC, and JOBS Act advocates in the legislature. Title II is much simpler in form, but it has been as controversial, if not more controversial, than any other part of the Act. Much in the way that Title I created a blurry line between public company status and private company status through adoption of the Emerging Growth Company definition, Title II creates a blurry line between public offers and private offers. Title II allows for the use of general solicitation and general advertising in the context of Rule 506 offerings and Rule 144A offerings, yet such offers are still considered "private."[83]

Title II of the JOBS Act required rule-making by the SEC, and on August 29, 2012, it put forth a release with a proposed SEC rule on general solicitation and general advertising.[84] Thereafter, the SEC received extensive and impassioned commentary from the public. Title II contains two key components: first, it authorizes issuers to generally solicit and generally advertise even in private offers, and second, it places an attendant obligation upon issuers to verify that persons receiving private offers are accredited investors.

In Rule 506 offerings, issuers can sell their securities to an unlimited number of "accredited investor[s]" without the offer being considered a public offer.[85] However, until passage of the JOBS Act, they could not recruit investors through "any form of general solicitation or general advertising."[86] Title II of the JOBS Act required the SEC to remove this ban on the use of general solicitation or general advertising in Rule 506 offerings.[87] The flip side of the issuer's newfound ability to solicit or advertise, how-

83. *See* JOBS Act, *supra* note 34, at § 201(a).

84. Proposed Rule Eliminating the Prohibition Against General Solicitation and General Advertising in Rule 506 and Rule 144A Offerings, Securities Act Release No. 33,9354, 77 Fed. Reg. 54,464 (proposed Aug. 29, 2012) [hereinafter Proposed Rule on General Solicitation].

85. 17 C.F.R. §§ 230.506(b), 230.501(e).

86. 17 C.F.R. §§ 230.506(b), 230.502(c); *see also* JOBS Act, *supra* note 34, at § 201(a)(1).

87. JOBS Act, *supra* note 34, at § 201(a)(1).

ever, is that such issuers must "*take reasonable steps to verify* that purchasers of the securities are accredited investors."[88]

Previously, issuers participating in Rule 506 offerings only had to have a "*reasonab*[*le*] belie[f]" that the purchasers were accredited investors.[89] The SEC's final rule—released just prior to this article going for publication—allows issuers to continue to conduct offerings that do *not* make use of general solicitation (under Rule 506(b)), while only subjecting issuers to the "reasonable belief" standard.[90]

Secondly, Title II removes the ban on general solicitation and advertising in the context of Rule 144A offerings.[91] While securities sold in the US private markets typically have restrictions on when they can be resold, 144A offerings allow for the immediate resale, as long as that resale is to certain institutional buyers.[92] Because there is not a time restriction on when the purchaser is allowed to resell the securities, the issuer of the securities gets a better price when it first sells the securities.[93] Rule 144A offerings have become an extremely popular way for companies to raise capital, and are particularly attractive to foreign issuers because—as "private" offerings—the issuer can avoid the public company reporting scheme of the United States.[94] Under the JOBS Act amendments, sellers in Rule 144A offerings can now use general solicitation and general advertising, provided they have a reasonable belief that the purchaser of the securities is an accredited investor.[95]

After releasing the Proposed Rule on General Solicitation and General Advertising, the SEC allowed for the common practice of accepting public commentary on the proposed rule. As mentioned, the SEC received much commentary on the proposed rules regarding general solicitation and general advertising. The views have varied widely between a diversity of interest groups, and the following provides only a small sample of the responses.

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88. *Id.* (emphasis added).

89. 17 C.F.R. §§ 230.506(b), 230.501(a) (emphasis added).

90. Proposed Rule on General Solicitation, *supra* note 84, at 54,467 (stating that issuers who do not wish to make use of general solicitation will not "become subject to the new requirement to take reasonable steps to verify the accredited investor status of purchasers"); *see also* Eliminating the Prohibition Against General Solicitation and General Advertising in Rule 506 and Rule 144A Offerings, Securities Act Release No. 33,9415, 78 Fed. Reg. 44,72 (July 10, 2013) [hereinafter Eliminating the Prohibition Against General Solicitation].

91. JOBS Act, *supra* note 34, at § 201(a)(2); 17 C.F.R. § 230.144A(d)(1) (2013).

92. William K. Sjostrom, Jr., *The Birth of Rule 144A Equity Offerings*, 56 UCLA L. Rev. 409, 410–11 (2008); *see also* Sec. and Exch. Comm'n. *SEC Final Rule: Resale of Restricted Securities; Changes to Method of Determining Holding Period of Restricted Securities Under Rules 144 and 145*, 55 Fed. Reg. 17933–01 (Apr. 30, 1990) (stating that resale of securities to "qualified institutional buyers" are exempt from the registration requirement of the Securities Act of 1933).

93. Sjostrom, *supra* note 92, at 411.

94. *Id.*

95. JOBS Act, *supra* note 34, at § 201(a)(2).

The Angel Capital Association (ACA) submitted a comment to the SEC that was in part praiseworthy, and in part critical, of the SEC's proposed rule.[96] Notably, it praised the SEC for maintaining Rule 506(b) in its current form, as this allowed for uninterrupted practice of Rule 506 offers that do not involve general solicitations.[97] The ACA continued, "[t]his supports the continued flow of capital for many job-creating startups, as was the intent of the JOBS Act."[98] The ACA's critique of the proposed rule was that it thought the SEC should have put forth more guidance regarding what constitutes "reasonable steps to verify" whether an investor is indeed accredited.[99] Although the SEC provided factors that would be relevant in determining what constitutes "reasonable steps to verify,"[100] the ACA comment suggested that the SEC should have created specific safe harbors so that if companies took particular steps, they could be assured that they had adequately verified the investor's status.[101] The ACA expressed concern that the "current proposed rules will lead to confusion and cause legal advisors to issuers to insist on complex and burdensome forms and submissions that will cause many angels to back away from this essential asset class."[102]

Another comment came from the Council of Institutional Investors (CII) which also expressed concern over the SEC's "failure to specify the verification methods" by which an issuer must ensure that an investor is accredited.[103] Additionally, the CII noted that the definition of an accredited investor—which for natural persons is based on having an income of $200,000 or a net worth of $1,000,000—is itself antiquated and based on quantitative thresholds established in the early 1980s.[104] Given that the financial thresholds to reach accredited status are rather attainable for natural persons, the CII thought the SEC's failure to put forth "strong safeguards" to ensure accredited status is likely to lead to more fraudulent activity.[105]

The North American Securities Administrators Association, Inc. (NASAA) is a group of "state securities regulators who work closely with small businesses in their capital formation efforts," and it also submitted a

96. Letter from Marianne Hudson, Exec. Dir., Angel Capital Ass'n to Elizabeth M. Murphy, Sec'y U.S. Sec. and Exch. Comm'n (Sept. 27, 2012), http://sec.gov/comments/s7-07-12/s70712-72.pdf [hereinafter ACA Comment].

97. *Id.*

98. *Id.*

99. *Id.*

100. *See* Proposed Rule on General Solicitation, *supra* note 84, at 54,467–71.

101. ACA Comment, *supra* note 96.

102. *Id.*

103. Letter from Jeff Mahoney, Gen. Counsel, Council of Institutional Investors, to Elizabeth M. Murphy, Sec'y, U.S. Sec. and Exch. Comm'n at 2 (Sept. 27, 2012), http://sec.gov/comments/s7-07-12/s70712-74.pdf [hereinafter CII Comment].

104. *See id.* at 3 (as a slight correction of the Council of Institutional Investors comment, an accredited investor is a natural person with a $200,000 annual income ($300,000 for married couples) *or* a net worth of $1,000,000). 17 C.F.R. §§ 230.501(a)(5), (6) (2013).

105. CII Comment, *supra* note 103, at 3.

comment regarding the proposed rule.[106] In its comment letter, the NASAA said it was "greatly disappointed" with the Rule 506 changes.[107] It felt that the SEC could have implemented the Rule 506 changes in a manner that was faithful to the intent of Congress, but would have provided much greater investor protection.[108] Primarily, the NASAA advocated for a rule that would require an issuer to make a regulatory filing before it engaged in any type of general solicitation or advertisement, as opposed to the current rule which requires issuers to make the filing fifteen days *after* the first sale.[109] Such a rule would put the burden on issuers to become compliant with SEC rules before advertising to investors, while the current rule places risk on the investor prior to the issuer certifying its compliance with SEC solicitation and advertising rules. The NASAA, similar to the ACA and the CII, also argued that the SEC should have provided specific "non-exclusive safe harbors for the verification of accredited investors."[110]

Conversely, the prominent New York City law firm of Sullivan & Cromwell submitted a comment to the SEC in which it largely praised the proposed rule.[111] In particular, it approved of the Commission's decision to apply a "facts and circumstances" standard to determine whether issuers took reasonable steps to verify an investor's status, as opposed to prescribing specific verification methods.[112] The law firm argued that the set of factors that the SEC put forward in its proposing release provided "a flexible and practical framework."[113] The firm argued, in opposition to the above groups, that "prescribed verification methods would be overly burdensome in some cases, while ineffective in others."[114]

After a lengthy period in which it accepted public commentary, the SEC in its final rule decided to create a series of safe harbor provisions that would satisfy an issuer's duty to take reasonable steps to verify accredited investor status.[115] The safe harbors will apply in four circumstances: where the issuer has gathered certain IRS documents of the investor; where the issuer has determined the net worth of an investor through the use of spe-

106. Letter from A. Heath Abshure, President, North American Sec. Adm' Ass'n, Inc., to Elizabeth M. Murphy, Sec'y, U.S. Sec. and Exch. Comm'n, at 1 (Oct. 3, 2012), http://www.sec.gov/comments/s7-07-12/s70712-92.pdf.

107. *Id.* at 2.

108. *Id.* at 10.

109. *Id.* at 3–5 (discussing the requirements for Form D submissions).

110. *Id.* at 5.

111. *See generally* Letter from Sullivan & Cromwell LLP to Elizabeth M. Murphy, Sec'y, U.S. Sec. and Exch. Comm'n (Oct. 5, 2012) (expressing approval and agreement with various approaches taken by the SEC), http://www.sec.gov/comments/s7-07-12/s70712-115.pdf.

112. *Id.* at 2.

113. *Id.*

114. *Id.* (listing some of the relevant factors put forward by the SEC: "nature of the purchaser, information about the purchaser available to the issuer and the nature and terms of the offering, and [ ] the interconnectivity of these factors").

115. Proposed Rule on General Solicitation, *supra* note 84 at 54,467.

cific documents, including, but not limited to bank statements or brokerage account statements; where certain professionals, including, but not limited to, investment advisers, accountants, or attorneys, can confirm that a person is an accredited investor; and lastly, where a person has previously invested with the issuer under Rule 506 as an accredited investor and the person can confirm that he or she is still an accredited investor.[116] These safe harbors are in addition to the "principles-based" method of verification from the proposed release,[117] and thus, the SEC forged a compromise between the above-mentioned parties that submitted commentary to the SEC. The accredited investor verification methods are relevant to capital market competitiveness because the perceived level of investor protection within a particular market can affect where an investor will bring his or her capital. Some investor advocates, such as the ACA, argue that the lack of clarity in the proposed verification rules will add costs to such an extent that angel investors may back away from Rule 506 offerings.[118] Relatedly, the SEC's proposing release acknowledged that a flexible verification standard could lead to legal uncertainty and add cost to issuers and investors in the form of litigation risk.[119] The SEC also warned that regardless of what shape the investor verification rules take, investor verification will add costs to the private placement market and could therefore dampen its attractiveness.[120] In its final rule on general solicitation and advertising, the SEC put forth a solution that would remain flexible, but also set forth some predictable standards. This should assuage investor protection concerns without adding costs and procedural layers to issuers conducting a Rule 506 offer.

The final form of Rule 506 makes an already strong private placement market even stronger. With the ability to generally solicit and advertise, issuers of securities have another tool in their belts, one that provides a means to offer securities without having to register as a public company. Given that "accredited investor" quantitative benchmarks for natural persons have not changed for thirty years,[121] in conjunction with the ability to generally advertise and solicit, issuers will have a continually growing market of potential investors that can participate in private offerings. Additionally, the SEC exercised sound judgment by maintaining Rule 506(b) offerings as they have traditionally been executed, thus not requiring issuers to verify whether an investor is accredited if the issuer does not generally advertise or solicit.[122] This should prevent interruptions for issuers and investors who already have successful investment relationships established.

116. *Id.* at 54,468–69.
117. *Id.* at 54,469.
118. *See* ACA Comment, *supra* note 96.
119. *See id*.
120. *See* Proposed Rule on General Solicitation, *supra* note 84, at 54,478.
121. *See* CII Comment, *supra* note 103, at 3.
122. *See* Proposed Rule on General Solicitation, *supra* note 84, at 54,467.

These groups can choose to avoid altogether offerings that make use of general solicitation, or can enter the market at a later date as the offering process is refined and made more efficient.

The demand for efficiency is what drives the private offering market. Issuers want to raise large amounts of capital quickly and with low costs. Today, the private offering market in the United States is an increasingly powerful source of capital for corporations.[123] Consider the following from the SEC's proposed release on the general solicitation rules:

> In 2011, the estimated amount of capital (including both equity and debt) raised in Rule 506 offerings and Rule 144A offerings was $895 billion and $168 billion, respectively, compared to $984 billion raised in registered offerings. In 2010, the estimated amount of capital (including both equity and debt) raised in Rule 506 offerings and Rule 144A offerings was $902 billion and $233 billion, respectively, compared to $1.07 trillion raised in registered offerings. These data points underscore the importance of the Rule 506 and Rule 144A exemptions for issuers seeking access to the U.S. capital markets.[124]

With a private offering market roughly the same size as the public offering market, and the main provision of Title II of the JOBS Act allowing general solicitation and advertising in two already popular markets, the widespread participation in private markets should continue to grow. This will bolster the size of US capital markets on the whole. However, Title II detracts from the broader goal of promoting more IPO activity. Both foreign and domestic issuers, having been given the freedom to generally solicit and advertise, will have increased access to capital without having to conduct a public offering. In turn, they will likely take advantage of this capital instead of subjecting themselves to the costs of an IPO and the disclosure obligations attendant to public company status.

C. *Title V: Private Company Flexibility and Growth*

Lest the private markets needed any more help, the JOBS Act incorporated Title V, bearing the name "Private Company Flexibility and Growth."[125] Like the IPO provisions in Title I, Title V was effective immediately; however, unlike Title I, Title V is concise and straightforward. Title V amends section 12(g)(1)(A) of the Securities Exchange Act to read that an issuer will be required to register as a public company when it has a class of securities held of record by at least 2,000 persons, or 500 persons who are not accredited investors.[126] Previously, an issuer was required to register

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123. *See Measure 7 – Relative Size of the Private Rule 144A and Public Equity Markets*, *supra* note 27.

124. Proposed Rule on General Solicitation, *supra* note 84, at 54,465–66.

125. *See* JOBS Act, *supra* note 34, at Title V.

126. *See id.* at § 501; *see also* 15 U.S.C. § 78l(g)(1)(A) (2012).

its securities once it reached 500 investors, regardless of whether or not the investors were accredited.[127] Now, a company can expand its investor base by as much as 1,500 investors (so long as 1,500 of the total investors are accredited) without having to file as a public company. Most notably in regard to section 12(g)(1)(A) is that the shareholder threshold refers to the number of shareholders "of record."[128] As Pritchard describes, "if broker-dealers held the shares on the company's record books as nominees for their customers, companies could have thousands of beneficial owners hidden beneath a record shareholder number that remained under 500."[129] With that 500 shareholders of record limit now raised to 2,000 shareholders of record, the effect that Pritchard describes is now compounded.

There is little professional commentary on this provision of the JOBS Act, and those who have commented have found it to be of minimal significance. This is primarily because of the shareholder "of record" distinction. In regards to becoming public through the shareholder ceiling of section 12(g), scholars Donald Langevoort and Robert Thompson note: "While roughly a size test, it is not really: as the Facebook example . . . show[s], many extraordinarily large and powerful companies have few enough record shareholders to avoid registration."[130] Pritchard was also doubtful of Title V's impact, stating, "I question whether this is an important constraint for companies smaller than Facebook that are striving to maintain their private status. Data on this issue are simply not available."[131]

Therefore, although the implication may be minimal for the majority of companies considering public versus private status, the minimal impact of the change nonetheless supports a company's ability to stay private. For example, Facebook's COO said that her company would not have gone public at the time it did if it had access to the 2,000 shareholder ceiling instituted by Title V of the JOBS Act.[132] Underscoring the increasing ability of US companies to remain private, it is remarkable that a company whose worth was estimated at more than $82 billion just months before its initial public offering[133] could potentially have remained private if the JOBS Act were enacted two years earlier.

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127. *See* 15 U.S.C.S. § 78l (2012) (describing in the annotations, under the section titled "Amendments," each amendment to Section 78l, including the text of § 78l(g)(1) as it appeared prior to the 2012 amendments).

128. *See* JOBS Act, *supra* note 34, at § 501; *see also* 15 U.S.C. § 78l(g)(1)(A) (2012).

129. Pritchard, *supra* note 2, at 1004.

130. Langevoort & Thompson, *supra* note 78, at 355 (citing Robert C. Bartlett III, *Going Private but Staying Public: Reexamining the Effect of Sarbanes-Oxley on Firms' Going-Private Decisions*, 76 U. Chi. L. Rev. 7, 11 (2009)).

131. Pritchard, *supra* note 2, at 1009.

132. Michelle Quinn & Jonathan Allen, *Facebook: JOBS Act Would Have Affected IPO*, Politico (Apr. 6, 2012, 3:43 PM), http://www.politico.com/news/stories/0412/74918.html.

133. Dealbook, *Tracking Facebook's Valuation*, N.Y. Times (Feb. 1, 2012, 1:20 PM), http://dealbook.nytimes.com/2012/02/01/tracking-facebooks-valuation/.

Similar to Title II, Title V gives issuers flexibility to stay private while increasing their access to new capital. To the extent that this is a gain for private companies, it is a loss for public markets. The impact of Title V could be stratified because the increased shareholder ceiling coincides with an issuer's increased ability to find additional investors by means of general advertising and solicitation. The JOBS Act provisions that collectively benefit private markets will do so to the relative detriment of US public markets.

Conclusion

The purpose of this paper is to consider whether the JOBS Act is likely to improve the competitive position of US capital markets. Answered simply, I conclude that the JOBS Act is likely to bolster America's capital markets overall, particularly because it strengthens the already robust private placement market. However, I do not think that the JOBS Act is likely to be effective in achieving its stated purpose, which was, "[t]o increase American job creation and economic growth by improving access to the *public* capital markets for emerging growth companies."[134] Key to this analysis is that while Title I of the JOBS Act might indeed make incremental steps to improve access to public markets, the remainder of the Act promulgates more influential measures that will strengthen the private markets, and thereby give companies the flexibility and even the incentive to remain private. This could nullify, or perhaps cause a net loss, to the relative strength of American public markets, despite gains the public markets achieved through Emerging Growth Company definition in Title I of the Act.

Limiting the availability of Emerging Growth Company status to newly public companies, and the decision by Congress to limit that status to a five-year period, regardless of size, are the major weaknesses in the JOBS Act—at least in relation to its stated objective. The "on-ramp" in Title I streamlines the IPO process and decreases reporting costs, causing issuers to go public earlier than they might have otherwise. The limited duration of their EGC status, however, should also incentivize them to wait, knowing that they have to project whether they will be able to afford full public company status five years later.[135] And—as discussed throughout this paper—these companies can more easily wait to conduct their IPOs, while still having access to capital, because the remainder of the JOBS Act grants flexibility and expansion of the investor pool for private offers.

134. *See* JOBS Act, *supra* note 34 (emphasis added).

135. For an illustration, if a company were to go public as an EGC when it had revenues of $400,000,000, assuming 20% annual growth in each of the next five years, it would reach revenues of $995,328,000 after five years. Thus, an EGC projecting relatively ambitious revenue growth would have to wait to do its IPO until it surpasses $400,000,000 in annual revenue if it wants to avoid being timed out of EGC status.

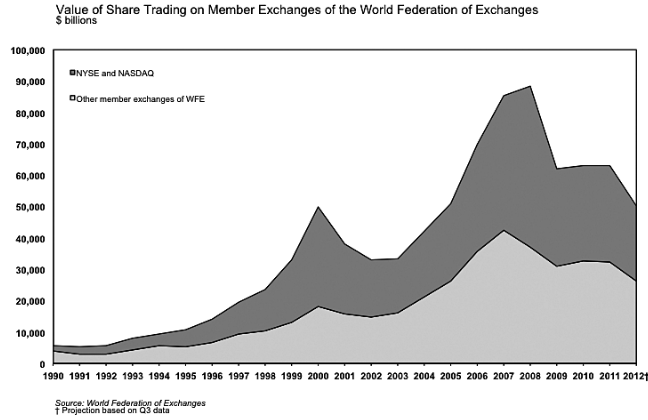
American private placement markets are already extremely active, and are only made more attractive to issuers through the Act. Under Title V, an issuer can now quadruple its investor base in the US without having to register its securities. Meanwhile, the general solicitation and general advertising provisions in Title II provide an avenue by which issuers can seek out accredited investors. The result is that both foreign and domestic issuers have increased access to capital in the United States, which they can access without absorbing the added costs of conducting an IPO or availing themselves to public company disclosure requirements. These provisions in tandem frustrate the purpose in Title I, which is to encourage companies to tap the public market.

The other key issue of the JOBS Act, which was not the focus of this paper, is that it is a loss for investor protection advocates. In this paper I did not endeavor to analyze the extent of the loss, but investor protection advocates gain next to nothing in each of the Titles discussed. Title I allows for less rigorous audit standards and less shareholder participation in corporate governance issues. Title II adds wording that requires issuers to verify accredited investor status, but this comes at the cost of issuers being able to advertise and solicit the public, in furtherance of "private" offers. Finally, Title V allows issuers to stay private for a longer period of time, and thus not be required to make periodic disclosures to the public.

Some observers are justifiably apprehensive that investor protection concerns will in fact lessen the attractiveness of US capital markets and drive investors away. Though I accept this argument, I do not anticipate investor protection shortcomings in the JOBS Act slowing down the wave of issuers who want access to the rapidly growing American private placement market. Whether or not the JOBS Act is prudent in regard to weighing investor protection against attractiveness of American capital markets, I leave for another to conclude. I do, however, anticipate that the Act will be effective in driving more activity in the US private placement market. As for the IPO on-ramp: I am skeptical that there will be traffic jams there any time soon.

APPENDIX A—US SHARE OF THE VALUE OF GLOBAL SHARE TRADING

Measure 11 - U.S. Share of the Value of Global Share Trading



Value of Share Trading on Member Exchanges of the World Federation of Exchanges

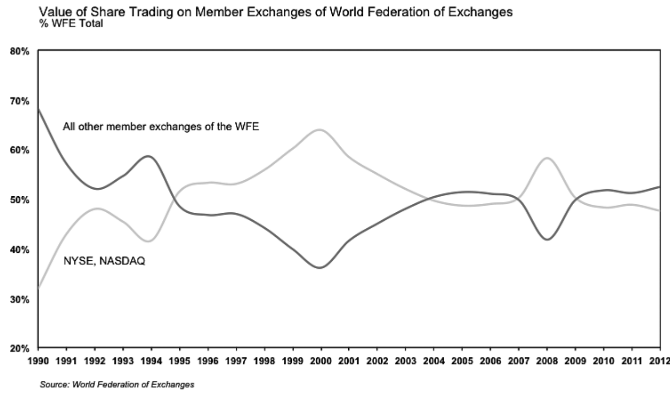
($ billions)																								CAGR*	
	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012†	1990-2002	2002-2012
NYSE**, NASDAQ	1,815	2,255	2,679	3,676	3,962	5,554	7,457	10,403	13,125	19,890	31,804	22,241	18,207	17,323	20,976	24,820	34,199	42,879	51,493	31,129	30,455	30,751	23,896	21.2%	2.6%
% of WFE Total	*32.0%*	*42.9%*	*48.0%*	*45.4%*	*41.6%*	*51.5%*	*53.2%*	*53.0%*	*55.8%*	*60.1%*	*63.9%*	*58.4%*	*55.0%*	*52.0%*	*49.6%*	*48.6%*	*49.0%*	*50.2%*	*58.2%*	*50.2%*	*48.3%*	*48.8%*	*47.6%*		
Other member exchanges of WFE	3,866	3,000	2,907	4,421	5,565	5,230	6,547	9,214	10,377	13,184	17,979	15,850	14,910	16,008	21,291	26,214	35,631	42,472	36,953	30,875	32,636	32,244	26,334	11.9%	5.6%
% of WFE Total	*68.0%*	*57.1%*	*52.0%*	*54.6%*	*58.4%*	*48.5%*	*46.8%*	*47.0%*	*44.2%*	*39.9%*	*36.1%*	*41.6%*	*45.0%*	*48.0%*	*50.4%*	*51.4%*	*51.0%*	*49.8%*	*41.8%*	*49.8%*	*51.7%*	*51.2%*	*52.4%*		
WFE Total	5,682	5,255	5,586	8,097	9,527	10,784	14,004	19,616	23,502	33,075	49,783	38,091	33,117	33,331	42,266	51,034	69,830	85,352	88,446	62,004	63,091	62,994	50,230	15.8%	4.0%

Source: World Federation of Exchanges

* Compound Annual Growth Rate

** NYSE acquired AMEX in 2008

† Projection based on Q3 data



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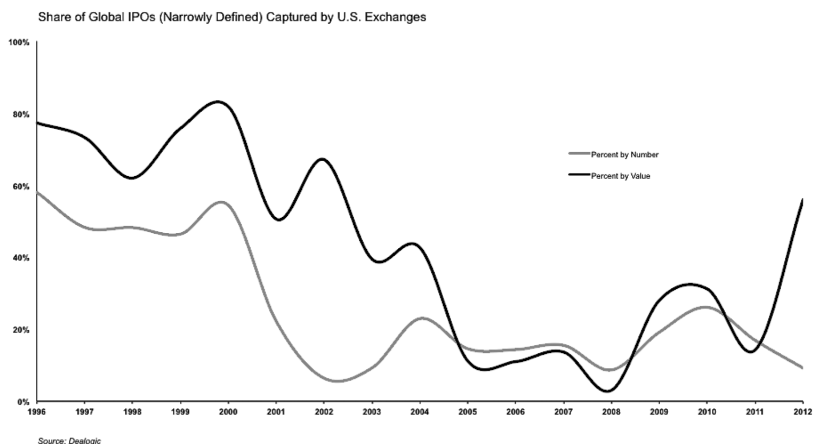
Appendix B—Global IPOs by Foreign Companies (Narrowly Defined)

Measure 2 - Global IPOs by Foreign Companies (Narrowly Defined)



Share of Global IPOs (Narrowly Defined) Captured by U.S. Exchanges

	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
Total Number of Global IPOs	105	118	85	112	136	45	47	54	122	192	237	335	92	99	207	130	76
Number of Global IPOs That Listed on a U.S. Exchange	61	57	41	52	74	10	3	5	28	28	34	52	8	19	54	22	7
% of Total Number	***58.1%***	***48.3%***	***48.2%***	***46.4%***	***54.4%***	***22.2%***	***6.4%***	***9.3%***	***23.0%***	***14.6%***	***14.3%***	***15.5%***	***8.7%***	***19.2%***	***26.1%***	***16.9%***	***9.2%***
($ billions)																	
Total Value of Global IPOs	32.3	46.8	25.2	45.4	43.1	15.1	3.7	12.4	21.5	40.5	97.8	95.8	20.9	36.9	79.8	39.3	9.0
Value of Global IPOs That Listed on a U.S. Exchange	24.9	34.3	15.6	34.4	35.3	7.6	2.5	4.9	9.2	4.5	10.8	13.1	0.6	10.3	24.9	5.6	5.1
% of Total Value	***77.3%***	***73.3%***	***62.0%***	***75.8%***	***81.8%***	***50.6%***	***67.1%***	***39.5%***	***42.7%***	***11.2%***	***11.0%***	***13.7%***	***3.0%***	***28.0%***	***31.2%***	***14.3%***	***55.9%***

Source: Dealogic

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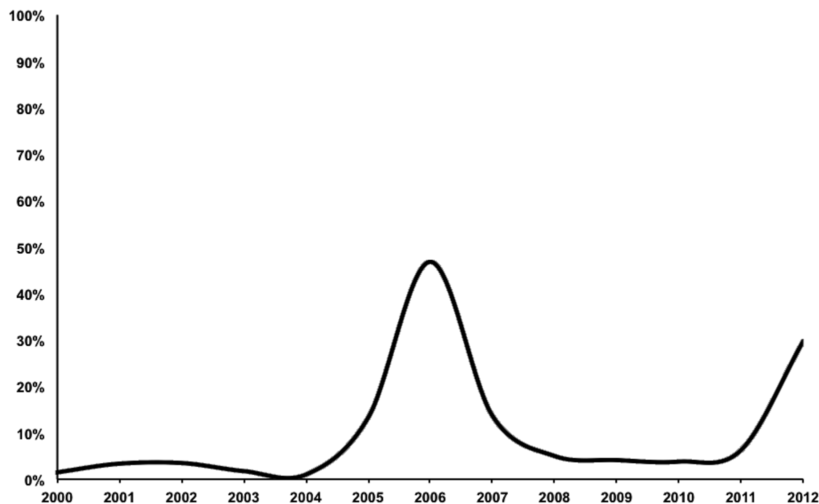
APPENDIX C—RELATIVE SIZE OF THE PRIVATE RULE 144A AND PUBLIC EQUITY MARKETS

Measure 7 - Relative Size of the Private Rule 144A and Public Equity Markets

Equity Raised in the U.S. by Foreign Issuers via 144A ADRs as a Percentage of Equity Raised in the U.S. by Foreign Issuers in the Public Market



Source: BNY Mellon and Thomson Reuters

Equity Raised by Foreign Issuers in the U.S. via Rule 144A ADRs and in the Public Market

($ billions)

	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
Equity Raised by Foreign Issuers in the U.S. via Rule 144A ADRs*	$0.267	$0.660	$0.567	$0.257	$0.225	$3.609	$9.878	$4.477	$0.308	$0.738	$0.771	$1.323	$4.759
Equity Raised by Foreign Issuers in the U.S. in the Public Market**	$17.244	$19.607	$16.158	$14.552	$22.006	$27.200	$21.086	$32.700	$6.151	$17.845	$20.229	$21.010	$15.996
144A ADRs as a % of Equity Publicly Raised by Foreign Issuers in the U.S.	*1.5%*	*3.4%*	*3.5%*	*1.8%*	*1.0%*	*13.3%*	*46.8%*	*13.7%*	*5.0%*	*4.1%*	*3.8%*	*6.3%*	*29.7%*

** Source: BNY Mellon*
*** Source: Thomson Reuters*

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