

Wayne Brown Institute

RAISING MONEY IN UTAH

KEY LEGAL ISSUES

# OVERVIEW

➤ General Principles

➤ Securities Laws

➤ Conclusion

# GENERAL PRINCIPLES:

## Business Entity

- Use appropriate structure
- Organize in Utah or Delaware
- Tax Considerations
- Prepare Business Plan

# GENERAL PRINCIPLES:

## Capitalization

- Demonstrate you know how successful companies are funded
- In Articles of Incorporation, establish “blank check” preferred stock and common stock
- Keep it simple
- Adopt stock option plan for key employees, advisors and others

# GENERAL PRINCIPLES:

## Capitalization

- Issue common stock to founders, seed investors and select key employees
- Use standard shareholders' agreement with "buy-back" or "cross-purchase" agreement
- Keep valuation of common stock realistic
- Limit number of shareholders
- Issue preferred stock to institutional and select angel investors

# GENERAL PRINCIPLES:

## Avoid Mistakes

- Know your investors
- Take money only from appropriate sources
- Retain and involve experienced legal, tax and accounting advisors
- Maintain appropriate records
- Comply with applicable laws and regulations

# SECURITIES LAWS:

## Overview

- Federal and state regulation
- Manner of offering; registration or exemption
- Anti-fraud rules
- Sales persons and finders

# SECURITIES LAWS:

## Definitions

- Security: Any stock, note, bond, debenture, interest or participation in profit-sharing arrangement, LLC interest, investment contract and any right or option to acquire the foregoing
- Accredited Investor: Directors and executive officers of the issuer; persons with net worth greater than \$1 million; persons with annual income greater than \$200,000 (or \$300,000 with spouse); organizations with assets greater than \$5 million

# SECURITIES LAWS:

## Registered Offerings

- **Public offering and distribution; general solicitation; shares freely transferable (except “affiliates”)**
- **Registration with SEC**
  - **Form S-1 (standard IPO)**
  - **Form SB-2 (“small business issuer”)**
  - **Form SB-1 (“small business issuer” up to \$10 million)**
  - **Form 1-A (most issuers up to \$5 million; no Securities Exchange Act of 1934 reporting and other obligations)**
- **State registration by coordination or qualification**

# SECURITIES LAWS:

## Exempt Offerings

- **Securities Act of 1933**
  - **Section 4(2) – Private transaction; facts and circumstances test**
  - **Section 4(6) – Private transaction; accredited investors only**
  - **Section 3(a)(11) – Intrastate transaction**
  - **Regulation D – Safe harbor for establishing exemption**
- **State exemptions – comparable or equivalent**

# SECURITIES LAWS:

## Regulation D

- Rule 504
- Rule 505
- Rule 506

# SECURITIES LAWS:

## Rule 504

- Unlimited number of purchasers
- Up to \$1 million in 12 month period
- General solicitation allowed if: (i) state registration requiring public filing and delivery of substantive disclosure document; or (ii) state law exemption from registration if offering made only to accredited investors
- Utah “blue sky” law provides for (i) state registration involving public filing and delivery of substantive disclosure document; and (ii) state exemption for accredited investors only with limited advertisement

# SECURITIES LAWS:

## Rule 505

- Unlimited number of accredited investors; up to 35 non-accredited investors
- Up to \$5 million in 12 month period
- No general solicitation
- No specific disclosure requirement for accredited investors; specific disclosures required for non-accredited investors
- Utah has parallel exemption

# SECURITIES LAWS:

## Rule 506

- **Unlimited number of accredited investors; up to 35 non-accredited investors (must meet “sophistication” requirement)**
- **No dollar limitation**
- **No general solicitation**
- **No specific disclosure requirement for accredited investors; specific disclosures required for non-accredited investors**
- **State law preempted by Rule 506 as “covered security”**

# SECURITIES LAWS:

## Anti-Fraud Rules

- Rule 10b-5 – No material misstatements or omissions
- State law rule (Utah Code Ann. § 61-1-1)
- Apply to all transactions involving sale of security

# SECURITIES LAWS: Sales Persons and Finders

- Federal and state registration as a “broker-dealer”
- Exemption for issuer agents
- Exemption for finders

# CONCLUSION

- Structure company, capitalization and transactions within accepted norms
- Comply with applicable securities laws
- Use experienced and professional legal, tax and accounting advisors
- Identify various sources of funding