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Take Your Company Public

Do you need to raise capital for your business? Do you want to increase the value of your company before you sell it? Are you looking for a way to expand you company? You may be a candidate to take your company public. Summit has partnered with the best in the industry to help you raise the capital you need and take your company public. We will show you how to **raise capital**, venture capital, do a **Direct Public Offering**, Regulation D 504 rules and raising small business financing.

Two common misconceptions about going public are that it is very expensive and that you must be as big as Microsoft to do it. These are not true. It is true that an IPO is very expensive but we are talking about a DPO, a Direct Public Offering. We will help you determine the best route but in many cases can do this program for about \$28,000 out of pocket spread out over many months.

So what are some of the benefits of going public?

- You will have more to work with when dealing with investors
- Your company will gain more recognition
- You may obtain financing more easily in the future if investor interest in your company grows enough to sustain a secondary trading market in your securities.
- The image of your company may be improved.
- Controlling shareholders, such as the company's officers or directors, may have a

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ready market for their shares, which means that they can more easily sell their interests at retirement, for diversification, or for some other reason.

- Your company may be able to attract and retain more highly qualified personnel if it can offer stock options, bonuses, or other incentives with a known market value.
- You can expand your business through stock acquisitions
- Seriously increase the value of your company before you sell

[Click here for a more complete list of benefits of going public](#)

There are many changes that will take place when going public with new obligations such as:

- You must continue to keep shareholders informed about the company's business operations, financial condition, and management, incurring additional costs and new legal obligations.
- You may be liable if you do not fulfill these new legal obligations.
- You may lose some flexibility in managing your company's affairs, particularly when shareholders must approve your actions.
- Your public offering will take time and money to accomplish.

Summit has many clients that are taking this route to financing, some clients have nothing more than a business plan in place. This can be used as a vehicle to raise the capital you need to launch your venture.

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Why Go Public?

There are a number of reasons to take your company public. (The process of registering a company's shares of stock with the Securities and Exchange Commission and offering the stock for sale to the public). Going public has both benefits and added responsibilities for your company. Some of the most compelling advantages include:

Access to capital: A public offering of stock can vary from 500,00 to over 1 billion. In 1999, 544 companies completed an IPO(Initial Public Offering). The total capital raised from these offerings was 23.6 billion. By offering stock for sale to the public a company can access a substantial source of corporate funding. If a company needs to raise capital, it can sell stock (equity) or it can issue bonds(debt securities). An initial equity offering can bring immediate proceeds to a company. These funds may be used for a variety of purposes including; growth and expansion, retiring existing debt, corporate marketing and development, acquisition capital and corporate diversity. Through a public offering founders suffer less dilution when raising capital. Once public, a company's financing alternatives are increased. A publicly traded company can return to the public markets for additional capital via a bond or convertible bond issue or secondary equity offering. A public status can also provide favorable terms for alternative financing from public and private investors. In general, public companies have a higher valuation than private enterprises.

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Liquidity: By going public, a company can create a market for its stock. In general, stock in a public company is much more liquid than stock in a private enterprise. Liquidity is created for the investors, institutions, founders, owners and venture capital professionals. Investors of the company may be able to buy or sell the stock more readily upon completion of the public offering. This liquidity can elevate the value of the corporation. The stock's liquidity is contingent on a variety of factors including, registration rights, lock-up restrictions and holding periods. A public company has greater opportunity to sell shares of stock to investors. Ownership of stock in a public company may help the company's principles to eliminate personal guarantees. Liquidity can also provide an investor or company owner an exit strategy, portfolio diversity, and flexibility of asset allocation.

Compensation: Many companies use stock and stock option plans to attract and retain talented employees. It is increasingly common to recruit and compensate executives with a combination of salary and stock. Stock in a public company can be issued as a performance based reward or incentive. This reward could be deemed desirable if the stock has a public market. Stock can be instrumental in attracting and keeping key personnel. Also, certain tax advantages are a consideration when issuing stock to an employee. Generally, capital gains taxes are lower than ordinary income taxes. Owners and employees may have specific restrictions relating to the liquidity and sale of the stock. A public offering can create a market for the company's stock. This market can result in liquidity and reward for the company's employees. A stock plan for employees demonstrates corporate good will allows employees to become partial owners in the company where they work. An allocation of ownership or division of equity can lead to increased productivity, morale and loyalty. This type of compensation is a way of connecting an employee's financial future to the company's success.

Prestige: A public offering of stock can help a company gain prestige by creating a perception of stability. A company's founders, co-founders and managers gain an enormous amount of personal

prestige from being associated with a client that goes public. Prestige can be very helpful in recruiting key employees and marketing products and services. When sharing ownership with the public, you spread the company's reputation and increase its business opportunities. By selling stock on an exchange your company can gain additional exposure and become better known. This exposure may lead to improved recognition and business operations. The public status can be leveraged when marketing goods and services. Often a company's suppliers and consumers become shareholders, which may encourage continued or increased business. In this example, a public company could have a competitive advantage over a private enterprise. An IPO can indicate credibility to a company's customers, which may lead to increased sales and a greater corporate profile. Once public, lenders and suppliers may perceive the company as a safer credit risk, enhancing the opportunities for favorable financing terms. Also, a public offering can create publicity that is effective when marketing your company.

Publicity: A public offering of stock can generate prestige, publicity and visibility, which is effective when marketing your company. Public companies are more likely to receive the attention of major newspapers, magazines and periodicals than a private enterprise. The proper use of press releases, interviews or news stories can increase investor awareness, shareholder value and demand for the stock. A strong ad campaign coupled with media initiatives can potentially increase sales and revenue. The publicity received from a public offering encourages new business development and strategic alliances. Analyst reports and daily stock market tables contribute to the awareness of the consumer and financial community. A successful public offering can get your company's story out to the world and open an opportunity for investors that are not suited for an investment in a private company. The publicity that a public offering brings can attract the attention of potential partners or merger candidates. Because the financial condition of a public company is subject to the scrutiny of the SEC reporting requirements, existing or future business relationships are strengthened. Tremendous exposure can be gained

from a combination of radio, television, print and IPO publicity.

Mergers and Acquisitions: Once a company is public and the market for its stock is established, the stock can be considered as valuable as cash when acquiring other businesses. A successful IPO can have a dramatic effect on a company's profile, perceived competitiveness and stability. This perception can lead to expanded business relationships and added confidence in the consumer. A valuation of a private company often reflects illiquidity. A successful public offering will increase a company's valuation leading to a variety of opportunities for mergers and acquisitions. With the ability to raise additional capital by returning to the public markets for another offering, a public company is better able to finance a cash acquisition. A public company also has the advantage of using the market's valuation when exchanging stock in an acquisition. SEC disclosure requirements offer merger candidates the assurance of shareholder scrutiny and accurate reporting of the financial condition or solvency of the public company. Using stock to acquire another company can be easier and less expensive than other methods. A public company's corporate strategy is outlined by annual reports and marketing brochures which encourages corporate growth, development and merger activity.

Exit Strategy: One of the important benefits of a public offering is the fact that the company's stock eventually becomes liquid, offering reward and financial freedom for the founders and employees. An IPO also creates a public market for the stock, which provides a potential exit strategy and liquidity to the investors. A psychological sense of financial success can be an added benefit of going public. A public offering can enhance the personal net worth of a company's shareholders. Even if a public company's shareholders do not realize immediate profits, public-traded stock can be used as collateral to secure loans.

Growing companies constantly need access to new capital. Going public is one way to obtain that capital, but it takes time and money -- quite a lot of both!

Going public offers some strategic advantages:

New Capital

Almost all companies go public primarily because they need money. All other reasons are of secondary importance. The typical (firm-commitment) IPO raises \$20-40M, but offerings of \$100M are not unusual. This can vary widely by industry.

Future Capital

Once public, firms can easily go back to the public markets to raise more cash. Typically, about a third of all IPO issuers return to the public market within 5 years to issue a "seasoned equity offering" (the term secondary is used to denote shares sold by insiders rather than by firms). Those that do return raise about three times as much capital in their seasoned equity offerings as they raised in their IPO.

Cashing Out

Although it is a bad signal to investors when an entrepreneur sells his own shares, it still makes sense for many entrepreneurs to cash out some of their equity in order to diversify their holdings or to enjoy life.

Mergers and Acquisition

Many private firms do not appear on the radar screen of potential acquirors. Being public makes it easier for other companies to notice and evaluate the firm for potential synergies.

Image

Public firms tend to have higher profiles than private firms. This is important in industries where success requires customers and suppliers to make long-term commitments. For example, software requires a significant investment in training and and no manager wants to buy software from a firm that may not be around for future upgrades, improvements, bug fixes, etc. Indeed, the suppliers' and customers' perception of company success is often a self-fulfilling prophecy.

Employee Compensation

Having a public share price makes it easy for firms to give employees a formal stake in the company.

There are also some disadvantages of going public that must be considered:**Profit-sharing**

If the firm is sitting on a highly successful venture, future success (and profit) has to be shared with outsiders. After the typical IPO, about 40% of the company remains with insiders, but this can vary from 1% to 88%, with 20% to 60% being comfortably normal.

Loss of Confidentiality

A major reason why firms resist going public is the loss of confidentiality in company operations and policies. For example, a company could be destroyed if the company were to disclose its technology or profitability to its competitors.

Reporting and Fiduciary Responsibilities

Public companies must continuously file reports with the SEC and the exchange they list on. They must comply with certain state securities laws ("blue sky"), NASD and exchange guidelines. This disclosure costs money and provides information to competitors.

Loss of Control

Outsiders are often in a position to take control of corporate management and might even fire the entrepreneur/company founder. While there are effective anti-takeover measures, investors are not willing to pay a high price for a company in which poor management could not be replaced.

IPO Expenses

An IPO is a costly undertaking. A typical firm may spend about 15-25% of the money raised on direct expenses. Even more resources are spent indirectly (management time, disruption of business).

Immediate Cash-out Usually Not Permitted

Typically, IPO entrepreneurs face various restrictions that do not permit them to cash out for many months after the IPO.

Legal Liability

All IPO participants in the coalition are jointly and severally liable for each others' actions. In

practice, this means that they can be sued for various omissions in the IPO prospectus when the public market valuation falls below the IPO offering price. Congress recently passed The Private Securities Litigation Reform Act of 1995. The Act protects disclosure of firm projections, and forces the suing shareholder to have a substantial participation in the firm. Although nothing can eliminate law suits, the Act reduces the likelihood of successful suits and thus influences settlement terms.

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The Process of Going Public

Section 5 of the Securities Act requires that a registration statement be filed with the SEC before securities are offered for sale to the public. It also prohibits the sale of those securities until the registration statement becomes "effective." (Although registration statements become public immediately upon filing with the Commission, it is illegal to sell the securities until the effective date.) The basic registration statement consists of two principal parts:

- **Part I**

Is the prospectus (the legal offering or "selling" document), which must be furnished to all purchasers of the securities. Your company - the "issuer" of the securities - is required to put in the printed prospectus the essential facts regarding its business operations, financial condition, and management. The prospectus must be made available to everyone who buys the new issue, and also to anyone who is made an offer to purchase the securities.

- **Part II**

Contains additional information available at the SEC for inspection by the public. (Copies of all disclosure documents filed with the SEC may be obtained by mail, for a nominal copying charge.)

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Basic Registration of Securities

The basic registration form is Form S- 1. It

requires companies to disclose, among other things:

- A description of the company's business;
- Its properties;
- Material transactions between the company and its officers and directors;
- Competition;
- Identification of officers and directors and their remuneration;
- Certain pending legal proceedings;
- The plan for distributing the securities; and
- The intended use of the proceeds.

It is not prepared as a fill-in-the-blank form like a tax return but is similar to a brochure, with information provided in a narrative format. There are also detailed requirements concerning financial statements, including the requirement that such statements be audited by an independent certified public accountant.

In addition to the information expressly required by the form, the company must also provide any other information necessary to make the statements complete and not misleading. If sufficient adverse or risk factors exist concerning the offering and the issuer, they must also be set forth prominently in the prospectus, usually in the beginning. Examples of these factors are:

Lack of business operating history; Adverse economic conditions in a particular industry; Lack of market for the securities offered; and Dependence upon key personnel.

Alternative Registration Forms for Small Business Issuers

Recently, the SEC adopted simplified forms (Forms SB- 1 and SB-2) for use by small business issuers. A small business issuer is a United States

or Canadian issuer that had less than \$25 million in revenues in its last fiscal year, provided that the value of its outstanding securities in the hands of the public is no more than \$25 million.

These formats are alternatives to Form S-1. Form SB-1 for small business issuers offering up to \$10 million worth of securities in a fiscal year, permits the use of disclosure similar to that required in a Regulation A offering, including the use of the question and answer format. It requires, however, audited financial statements.

Form SB-2 permits the offering of an unlimited dollar amount of securities by any small business issuer. The form may be used again and again as long as the issuer meets the definition of small business issuer. Form SB-2 offers certain advantages, including the location of all disclosure requirements in a central repository, Regulation S-B. These disclosure requirements are presented in simple, non-legalistic technology.

Form SB-2 also permits the issuer to:

- Provide audited financial statements, prepared in accordance with generally accepted accounting principles, for two fiscal years (Form S-1 requires the issuer to provide audited financial statements, prepared in accordance with more detailed SEC regulations, for three fiscal years);
- Include less extensive narrative disclosure, particularly in the areas of the description of business, and executive compensation, than that required by Form S-1; and
- File its initial public offering with either the SEC Regional Office nearest to where the company conducts its principal business operations (the Atlanta District Office for issuers in the Southeast Region) or with the SEC Division of Corporation Finance in Washington, DC. The primary advantage of regional filing is that regional office personnel may be more familiar with local economic conditions, the business community, the financial environment, and, in some cases, the background and history

of the company.

Registration statements are examined for compliance with disclosure requirements. If a statement appears to be materially incomplete or inaccurate, the registrant usually is informed by letter and given an opportunity to file correcting or clarifying amendments. The Commission can refuse or suspend the effectiveness of any registration statement if it finds that material representations are misleading, inaccurate, or incomplete.

If my company becomes "public," what are its disclosure obligations?

The Exchange Act requires a company to file certain periodic reports once its registration statement has been declared effective. This obligation continues indefinitely unless:

- At the beginning of any subsequent fiscal year, the class of securities offered is held of record by less than 300 persons; or
- At the beginning of any subsequent fiscal year (except the two fiscal years immediately succeeding the year the registration statement became effective), all securities offered are held of record by less than 500 persons and the issuer has had less than \$5 million in total assets for each of its last three fiscal years.

In these cases, the reporting obligation is suspended. Otherwise, a company must continuously disclose certain information about:

- Its operations;
- Its officers, directors, and certain shareholders (including salary, various fringe benefits, and inside transactions between the company and management);
- The financial condition of the business (including audited financial statements by an independent certified public accountant); and

- Its competitive position, material terms of certain contracts or lease agreements, etc.

All companies with total assets exceeding \$5 million and a class of equity securities held by 500 or more persons are required by the Exchange Act to file the same supplementary, periodic, and current reports as noted above. Companies with these characteristics must also comply with the Commission's proxy rules if proxies are solicited from holders of its securities. In such a case, the company must furnish all shareholders proxy statements disclosing all material facts concerning matters on which they are being asked to vote. If the proxy solicitation by management relates to an annual meeting at which directors are to be elected, the Commission's proxy rules also require the company to furnish each shareholder an annual report disclosing certain information about the company, including audited financial statements for its latest fiscal year.

Small business issuers are offered an alternative in the Commission's continuous reporting system. This alternative permits them to use Regulation S-B as the appropriate disclosure requirements for registration under the Securities Act, as well as registration and reporting under the Exchange Act.

Are there legal ways to sell securities without registering with the SEC?

Yes! The Securities Act provides several exemptions from the registration requirements; the most common are discussed below. Nonetheless, purchases or sales of securities (even in exempt transactions) are subject to the antifraud provisions of the federal securities laws. This means that issuers are responsible for false or misleading statements (whether oral or written) which may be redressed through private or government legal action, including criminal sanctions. Also, if all conditions of the exemptions discussed below are not met, purchasers may seek to have their purchase price refunded. In addition, the fact that an offending may be exempt from certain provisions of the federal securities laws does not necessarily mean that it is exempt from the notice and filing obligations of various state laws. Issuers

are cautioned to check with the appropriate state authority before proceeding with an offering relying on any of the exemptions discussed below.

Intrastate Offering Exemption

Section 3(a)(1) of the Securities Act is generally known as the "intrastate offering exemption." It exempts from registration any security which is part of an issue offered and sold only to residents of a single state or territory and the issuer is both a resident of and doing business within that state or territory. This exemption is intended to facilitate the local financing of local business operations. In order to qualify for the intrastate offering exemption, your company must:

- Be incorporated in the state where it is making the offering;
- Carry out a significant amount of its business in that state; and
- Make offers and sales only to residents of that state.

Although there is no fixed limit on the size of the offering or the number of purchasers, your company has the obligation to determine the residence of each purchaser. If any of the securities are offered or sold to one out-of-state purchaser, the exemption may be lost. In addition, if any of the securities are resold by an original resident purchaser to a person resident outside the state within nine months after the offering by the issuer is completed, the entire transaction may be in violation of the Securities Act. Therefore, there is usually no significant after-market for any securities issued in an intrastate offering during the nine-month period following the initial sale. Consequently, they must normally be sold at a discount.

It is difficult for you as an issuer to rely on the intrastate exemption unless your company knows the purchasers and the sale is directly negotiated with them. A company with some of its assets outside the state, or deriving a substantial portion of its revenues outside the state where it proposes

to offer its securities, will probably have a difficult time justifying the exemption.

The SEC has adopted Rule 147, a "safe harbor" rule, which may be followed by companies to be certain they meet the requirements for this exemption. It is possible, however, that transactions not meeting all requirements of Rule 147 may still qualify for the exemption.

Private Offering Exemption

Section 4(2) of the Securities Act provides exemption from registration for "transactions by an issuer not involving any public offering." There has been much uncertainty as to the precise limits of this private offering exemption. Generally, sales to persons who have access to information about the company and are able to fend for themselves (such as those directly managing the business) fall within the intended scope of the exemption. These are known as "sophisticated investors." As the number of purchasers increase and their relationship to the company and its management becomes more remote, however, it becomes more difficult for an issuer to demonstrate that the transaction does, in fact, qualify for the exemption.

To qualify the offering under this exemption, it is necessary that the persons to whom your company sells the security:

- Have sufficient knowledge and experience in financial and business matters that they are capable of evaluating the risks and merits of the investment (the "sophisticated investor"), or are able to bear the economic risk of the investment;
- Have access to the type of information normally provided in a prospectus; and
- Agree not to resell or distribute the securities.

In addition, your offering may not be made by any form of public solicitation or general advertising. You should be aware that if the security is offered for sale to even one person who does not meet the

necessary conditions, the entire offering may be in violation of the Securities Act. The SEC has adopted Rule 506, another "safe harbor" rule, which provides objective standards upon which business people may rely in order to be certain they meet the requirements of this exemption. Rule 506 is a part of Regulation D, which is described more fully later.

Regulation A

Section 3(b) of the Securities Act gives the SEC authority to exempt from registration certain offerings where the securities to be offered involve relatively small dollar amounts. Under this provision, the SEC has adopted Regulation A, a conditional exemption for certain public offerings not exceeding \$5 million in any 12-month period. An offering statement (consisting of a notification, offering circular, and exhibits) must be filed with the SEC Regional Office in the region where the company's principal business activities are conducted (the Atlanta District Office for issuers located in the Southeast Region). Although Regulation A is technically an exemption from the registration requirements of the Securities Act, it is often referred to as a "short form" of registration since the offering circular (similar in content to a prospectus) must be supplied to each purchaser and the securities issued are freely tradeable in an aftermarket.

The principal advantages of Regulation A offerings, as opposed to full registration on Form S- 1, SB- I or SB-2, are:

- Required financial statements are simpler and need not be audited; and
- There are no periodic SEC reporting requirements (other than sales reports following the sale of the securities) unless the issuer has more than \$5 million in total assets and more than 500 shareholders.

There are three permitted offering circular formats under Regulation A, one of which is a simplified question-and answer document. This style of disclosure is useful to potential investors and may

offer significant benefits to the issuer in the time expended and the costs of preparation.

All types of companies which are not reporting under the Exchange Act may use Regulation A, except "blank check" companies (i.e., those with the business of seeking an unspecified business) and investment companies registered or required to be registered under the Investment Company Act of 1940.

In most cases, Regulation A may also be used by shareholders for the resale of up to \$1.5 million of securities.

Regulation A includes a provision which allows an issuer to "test the waters" to determine whether or not there is any investor interest in its securities before the filing of a complete offering document. Thus, an issuer may publish factual information about its business or proposed business before incurring a full range of legal, accounting and other costs, in order to gauge potential investor interest in a possible securities offering; however, the provision specifically provides that no money may be solicited or accepted until an offering statement has been qualified by the Commission, and prescribed offering materials have been delivered to potential investors.

Regulation D

Under Sections 4(2) and 3(b) of the Securities Act, the SEC in March, 1982, adopted Regulation D to coordinate the various limited offering exemptions and to streamline the existing requirements applicable to private offers and sales of securities. The Regulation establishes three exemptions from registration in Rules 504, 505, and 506.

Rule 504

Rule 504, which provides an exemption for non-reporting companies unless they are "blank check" issuers, stipulates that:

The sale of up to \$1,000,000 of securities in a 12-month period is permitted; No limitation is placed on the number of persons purchasing securities; The offering may be made with general solicitation or general advertising; The securities received in the

offering are not "restricted securities"; and A Form D notice be filed with SEC headquarters within 15 days after the first sale of securities under the Rule.

Unlike Rules 505 and 506, Rule 504 does not mandate that specified disclosure be provided to purchasers. Nonetheless, the businessperson should take care that sufficient information is provided to meet the full disclosure obligations which exist under the antifraud provisions of the securities laws.

Rule 505

Rule 505 was adopted by the SEC to provide small businesses more flexibility in raising capital than under Rule 504 - but without the uncertainty of determining the quality of the purchasers that generally is involved in using Rule 506. Rule 505 provides issuers a limited offering exemption for sales of securities totaling up to \$5 million in any 12-month period.

Rule 505 contains certain restrictions regarding "accredited investors" and non-accredited persons. The-term "accredited investor" includes:

- Banks, insurance companies, registered investment companies, business development companies, or small business investment companies;
- Certain employee benefit plans for which investment decisions are made by a bank, insurance company, or registered investment adviser;
- Any employee benefit plan (Within the meaning of Title I of the Employee Retirement Income Security Act) with total assets in excess of \$5 million;
- Charitable organizations, corporations or partnerships with assets in excess of \$5 million;
- Directors, executive officers, and general partners of the issuer;
- Any entity in which all the equity owners are accredited investors;
- Natural persons with a net worth of at least \$1 million;
- Any natural person with an income in excess of \$200,000 in each of the two most recent years or joint income with a spouse in excess of \$300,000 for those years and a reasonable

expectation of the same income level in the current year; and

- Trusts with assets of at least \$5 million, not formed to acquire the securities offered, and whose purchases are directed by a sophisticated person.

There is no specific information the issuer must furnish to accredited investors. However, non accredited investors must be advised of and furnished, upon request, all material information furnished to accredited investors, as well as certain specified information.

Financial statement requirements include:

- Only financial statements for the most recent fiscal year need be certified by an independent public accountant;
- If an issuer other than a limited partnership cannot obtain audited financial statements without unreasonable effort or expense, only the issuer's balance sheet (to be dated within 120 days of the start of the offering) must be audited;
- Limited partnerships unable to obtain required financial statements without unreasonable effort or expense may furnish financial statements prepared on the basis of federal income tax requirements and examined and reported on by an independent public or certified accountant in accordance with generally accepted auditing standards; and The issuer must also be available to answer questions by prospective purchasers about the issuer or the offering.

Further restrictions under Rule 505 include:

- The total offering price of each issue of securities may not exceed \$5 million. .
- The offering may not be made by means of general solicitation or general advertising.
- The issuer may sell the securities to an unlimited number of "accredited investors" and to 35 nonaccredited persons. There are no requirements of "sophistication" or "wealth" for persons to whom the securities are sold.
- A company must take any necessary steps to ensure that the purchasers are acquiring securities for investment only, not for resale. The securities are thus "restricted" and investors must be informed that they may not be able to sell for at least two years.

- The issuer is not required to file any offering materials with the Commission. Fifteen days after the first sale in the offering, the issuer must file a notice of sales on Form D. The notice also contains an undertaking under this Rule for the issuer to furnish the Commission, upon its staff's request, any information given to non-accredited purchasers in connection with the offering.

Rule 506

Offers and sales of securities by an issuer that satisfy the conditions stated below are deemed transactions not involving any public offering within the meaning of Section 4(2) of the Securities Act. For an offering to be considered exempt from the registration requirements, Rule 506 stipulates:

- There is no ceiling on the amount of money which may be raised.
- No general solicitation or general advertising is permitted.
- The issuer may sell its securities to an unlimited number of accredited investors and 35 non-accredited purchasers. Unlike Rule 505, all non-accredited purchasers (either alone or with a purchaser representative) must be sophisticated - that is, have sufficient knowledge and experience in financial and business matters to render them capable of evaluating the merits and risks of the prospective investment.
- The term "accredited investor" is defined as above under Rule 505.
- There is no specific information which the issuer must furnish to accredited investors. However, non-accredited investors must be advised of and furnished, upon request, all material information furnished to accredited investors, as well as certain specified information.

The information requirements are generally the same as those on the registration form the issuer would be entitled to use. If the issuer cannot obtain audited financial statements without unreasonable effort or expense, then financial statements may be provided in accordance with the special treatment described under Rule 505 above.

The securities sold are "restricted" under the same stipulations in Rule 505.

A company is required to file a notice of the

offering on Form D at SEC headquarters within 15 days after the first sale in the offering. There is no requirement to file the offering memorandum with the Commission.

Accredited Investor Exemption: Section 4(6)

The Small Business Investment Incentive Act of 1980 created a new statutory exemption from registration under the Securities Act for transactions involving offers and sales of securities by any issuer solely to one or more "accredited investors." Under Section 4(6):

The total offering price of each issue of securities under the exemption may not exceed the limit on small offerings set by Section 3(b) the Securities Act, which currently is \$5 million per issue.

The offering may not be made by means of any form of advertising or public solicitation.

The term "accredited investor" is defined to include the same individuals and entities as included for purposes of Rules 505 and 506.

The issuer is required to file a notice of sales on Form D with the Commission 15 days after the initial sale is made in reliance on the exemption.

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The Need for Financing

Summit Business Brokers will assist in linking companies to capital and providing the services necessary to go public. Over years of experience we have found ourselves answering many of the same questions about financing - so we decided to put together this guide to help educate companies and individuals about the basics of business financing for companies that are planning for or considering going public.

Understanding the Need for Financing

The first question that must be answered prior to obtaining funds from another party is: "Why do you need the money?" There are many reasons why companies seek outside financing. This section covers the most common:

- 1) Growth Financing
 - a. Physical Expansion
 - b. Working Capital for Growth
 - c. Refinancing to Replace Restrictive Lenders
- 2) Acquisition Financing
 - a. Debt
 - b. Equity
 - c. Stock Swaps

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- 3) Turnarounds
- 4) Management Buyouts
- 5) Employee Buyouts
- 6) ESOP Financing
- 7) Internet Financing
- 8) Recapitalizations (Recaps)
- 9) Roll-Ups

Growth Financing

The most common use of financing is to fund a company's growth. Many companies reach a point in their growth where they need outside financing to expand to meet their potential. In this case, we assume that the current owners of the business are not seeking to liquidate some or all of their stake in the business, but rather are looking for financing to augment the cash flows of the company during a period of anticipated rapid growth. This growth can result from an expansion of the company's physical plant or through sales growth that requires additional working capital. The three most common reasons for needing access to growth financing are the following:

Physical Expansion

Physical expansion can be the easiest form of growth for a company to finance through outside sources. The company is normally increasing its asset base and therefore its borrowing capacity.

Expansion scenarios can be located on a spectrum. At one end of the spectrum is the project in which all of the costs are associated with the purchase of fixed assets. The most obvious example is the purchase of a new vehicle used in the core business of the company. These projects are good candidates for low-cost financing -- asset-backed senior debt being but one possibility. The rise of lease financing as a tool for businesses provides another low-cost, off-balance-sheet source of capital that in certain situations may enable the company to finance 100% of the cost of the asset.

Even if lease financing is not available, the company may be able to use some of its own excess borrowing capacity to collateralize that portion of the debt in excess of the amount a lender is willing to advance.

At the other end of this spectrum are projects in which a substantial portion of proceeds will be spent on soft costs, generating little in the way of fixed assets to collateralize the loan. If the company has little or no debt on its books, it may be able to use its borrowing base to fund the soft costs. If the company has borrowed against those assets for its own purposes and they are unavailable, the companies must turn to junior capital - equity or subordinated debt or both - to fill the gap.

Somewhere in the middle lie those situations in which the collateral values are too low to secure asset-backed financing for the entire transaction but in which the historic cash flows of the business are sufficient, or the likelihood that the expansion effort will succeed are so great, that a senior lender will make what is termed a cash flow loan. This loan, often structured with accelerated amortization and a cash flow sweep provision, is also referred to as an "air ball". The lender holds his or her breath for the period of time this loan is outstanding, hoping that those cash flows hold up and the loan is repaid. Cash flow loans are always more expensive than asset-backed, or secured loans, and are generally available from larger, more sophisticated banks and financial institutions.

Working Capital for Growth

In some situations, a company can grow without purchasing additional assets or expanding its physical plant. Often, this growth requires additional working capital to finance inventory purchases and accounts receivable that may grow faster than payables, putting the company in a tight cash position. Provided this growth follows historic patterns and is built on business relationships with customers roughly similar to the company's current customer base, an existing revolving line of credit can generally be expanded to accommodate the new credit needs of the

business.

In situations where the company is branching out into uncharted territory, or is contemplating growth that does not necessarily create a larger current asset base against which to borrow, the company may find itself in need of subordinated debt or equity. In those situations, the analysis the company will be subject to is identical to situations where they require subordinated debt and equity financing. The risks of the business as it is and the risks that the growth efforts will fail are weighed by a lender or investor relying on continued cash flows and equity growth to realize an appropriate return.

Refinancing to Replace Restrictive Lenders

There are situations when a company is poised for growth and is held back by a reluctant financial partner, most often but not exclusively a conservative bank unwilling to bear the risks of growth. Banks are often in the position of curbing growth if only because they generally do not price their loans to account for the risks associated with change. Particularly where the company will require both additional senior debt from the institution in question as well as junior capital which will complicate the company's balance sheet and introduce a new party into the lending relationship, the bank may elect to exit the loan.

The most important insight an entrepreneur can take into a refinancing situation is the fact that the same amount of senior debt can look very different depending on the other elements of the balance sheet, even without any changes in the company's base business.

Acquisition Financing

The opportunity to complete a strategic acquisition is one of the best ways to enhance the value of a company, since an acquisition may enable you to leap frog competitors, open new markets, develop new product lines, etc. However, a poorly executed acquisition can weaken a company's balance sheet and distract key management without providing the anticipated value.

All acquisitions have unique characteristics and, therefore, unique financing requirements. Much depends on the company being acquired (the "Target") and the Acquirer's strategy. We have highlighted below the three basic types of financing and their respective pros and cons. Depending on the financial health of both the Target and the Acquirer, the financial structure can be any combination of (i) debt, (ii) equity and (iii) the Acquirer's stock. Three primary issues to address when structuring the acquisition are:

1. The amount of debt which should be raised.
2. Creating a capital structure that is appropriate for the combined Company's future.
3. The cost of funds.

Debt Financing

Debt is the cheapest method of financing an acquisition bid and can take many forms. The amount of debt that can finance an acquisition depends on the projected cash flows of the combined Company. This will depend on the financial health of both the Target and the Acquirer.

If your company is interested in a leveraged buyout, it may be able to finance all or most of the purchase price with debt. Under this structure, the assets and cash flows of the Target collateralize the debt. This transaction is very similar to a home mortgage, where the underlying asset backs the loan.

Banks usually provide the cheapest and most common form of debt; senior debt. However, there are many other providers of senior debt who employ different methodologies for structuring loans. Subordinated debt lenders are more aggressive in the amount of debt they provide. Accordingly, these lenders charge higher interest rates and often require a piece of the equity of the combined company.

While debt is cheaper than equity, the interest and amortization requirements as well as possible financial covenants can limit a company's

flexibility. Large amounts of debt are more appropriate for mature companies with stable cash flows who will not require much capital for growth. Companies that foresee rapid growth, require substantial capital expenditures, and compete in turbulent markets are often better off financing acquisitions with more equity than debt.

Equity Financing

Equity is a more expensive form of capital than debt. This is because it carries the most risk since it has no claim to the company's assets. Acquisitions that have unstable cash flows, require capital for growth and compete in turbulent industries often require a greater amount of equity. Equity provides more financial flexibility because it does not require scheduled payments.

Financing an acquisition with equity requires relinquishing some amount of ownership in the combined company. The equity investors will often assume some amount of representation on the Board of Directors. Equity investors can take the form of leveraged buyout funds, venture capital funds or corporations.

Stock Swaps

It is also possible to use the Acquirer's stock to purchase all or some of the shares of the Target. This is very common among companies whose stock is publicly traded. A stock swap is more difficult in private transactions because the acquiring stock is illiquid (i.e. cannot be quickly sold). However, if the owner of the Target would like to retain some stake in the combined Company then exchanging shares is a sensible solution.

In order to complete a stock swap, a value must be placed on the equity of both companies and a share price must be determined. The investment banker on the Acquisition Team will be able to provide guidance in valuing both companies. There is a range of methods for valuing a private company, including:

- 1) Publicly traded comparable Company
Comparable Valuation Analysis

2) Comparable Transaction Valuation Analysis

3) Discounted Cash Flow Valuation Analysis

4) Leveraged Buyout Analysis Financial Buyer Valuation

A stock swap is a valuable tool for retaining the involvement and expertise of the Target's owner, if that is desired. If the owner is active in managing the Target's operations and his or her expertise is important to the success of the combined operation, offering stock in the combined company will insure that the interests of the two parties are aligned.

A stock swap often funds some portion of the purchase price in roll-up strategy acquisitions. Financing a roll up strategy usually requires an initial equity investment in the Acquirer to position it for rapid growth. Subsequent acquisitions are then financed largely with debt. However, stock in the combined company is an important currency to fund the purchase price, but also to retain the involvement of the management/owners of the Target.

Turnarounds

Turnaround financing involves providing capital to companies that are performing poorly but that are expected to turn around and perform much better in the future. Often this kind of financing occurs in the context of a transaction or purchase of the company by a new owner and often a new management team is hired at the same time. Turnaround financing can include Senior Debt, Subordinated Debt and Equity.

There are very few sources of Turnaround financing. Turnarounds involve companies that for one reason or another (or a combination of reasons, more often) have fallen on hard times. Someone sees value in the business beyond what is obvious from the current and recent performance and takes on the challenge of turning the business around. These opportunities are fraught with risk - typically, if the company continues on its present course, it will not be able

to remain a going concern; this is all the more true if the transaction that starts the turnaround involves debt financing. Against that backdrop - that the current state of affairs will lead to disaster - are the twin challenges of (a) accurately diagnosing what is wrong with the business and (b) quickly developing and implementing a turnaround plan that addresses those problems.

Management Buyouts

Managers often team up with private equity investors to purchase businesses or subsidiaries, divisions or product lines of corporations, using a combination of debt and equity financing. This is one of the most powerful methods for enriching the entrepreneurial spirit of professional managers.

Management buyouts represent the opportunity of a lifetime. After playing a critical role in building their company, managers often consider buying their company as the natural next step in the progression of the company's ownership. For most managers, a company buyout is the fulfillment of their dreams. However, successfully pursuing and implementing a management buyout is one of the most difficult jobs a manager will ever tackle.

Managers are experts at running their companies, but most managers have little experience making an acquisition. Management buyouts generally occur in a short time frame and require substantial and multiple sources of capital as well as legal, accounting, environmental and other professional support.

Employee Buyouts

Employee Buyouts are one of the most fascinating developments in the world of corporate finance. They had their beginnings in the early 1970s after Employee Stock Ownership Plan (ESOP) regulations were codified in the law as part of the ERISA legislation in 1974. An Employee Buyout involves owners of a company selling a majority of their stock to its employees through an ESOP structured corporate transaction.

Employee Buyouts can turn around failing companies, increase the cash flows of good

companies, motivate employees to outperform their competition, reduce or eliminate corporate taxes for years, and provide a tax-advantaged investment for employees. In the highest of capitalist traditions, Employee Buyouts can also transfer wealth in a free market transaction, to the employees who have spent their lives building the company.

ESOP Financing

Countless studies have shown that employee ownership motivates employees to improve their productivity, the quality of their work and the competitiveness of their company. ESOP Financing provides a whole series of benefits to the owners of a company, to the company itself and to the employees.

Leveraged ESOP Financing can allow an owner to sell all or a portion of his or her stock to the employees and indefinitely defer capital gains taxes. This has the added impact of reducing the company's taxes while it provides employees with tax sheltered ownership of the company's stock.

Internet Financing

Every company that deploys a product or service through a large and expensive distribution system will be confronted over the next ten years with a major distribution dilemma. Should the company continue to market through its existing distribution system or should it dramatically reduce costs by turning instead to the Internet to distribute and market its product or service? A direct market distribution strategy will require significant investment in expertise, structures and systems that many companies today cannot fathom. Additional funding may be required to make the business transition.

Recapitalizations

There are many situations in which a company may need to be recapitalized. As the word implies, a recapitalization involves an infusion of capital and, potentially, certain parties taking money out of the company. This occurs when a shareholder sells his or her stake in the company or when

existing debt providers are being replaced. In any recapitalization, the company must perform many of the same tasks as it would in an acquisition or buyout.

Rollups

A rollup is a strategy of buying several companies at once, or in rapid succession, in one industry to gain a variety of corporate benefits, such as economies of scale, broader product line, cheaper financing, greater diversity of customer base, etc. Rollups are very complicated transactions that should be implemented by a highly experienced team of professionals. Experienced sources of capital are critical to implement a rollup on the timetable necessary to achieve success. However, rollups can be considered to consist of a number of the above discussed transactions (or combinations thereof) executed within a narrow time horizon.

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Incorporating a Public Company

In deciding which state is the best state in which to incorporate, several factors must be analyzed. What is a state's regulatory climate? What is a state's tax situation? What is a state's stance on individual privacy? Which state will allow you the greatest stability to run your business the way you see fit? Which state has the best body of statute? Which states have the lowest filing fees?

For years, Delaware has been the leading state of choice for businesses wishing to incorporate. Delaware drafted an excellent body of statutory law. Delaware was very, very flexible and allowed ease of operation throughout the United States. But over the last few decades, a new state has risen and has taken Delaware's place as the preferred state for new businesses, and that state is Nevada. Let's consider several points and after we do, I am certain you will agree with me that Delaware is no longer the best state in which to incorporate.

First, Delaware has a franchise tax, Nevada does not.

Secondly, Delaware has an income tax, Nevada does not. While it is true that this 8.7% income tax applies only to revenue earned within Delaware, this may change. In any event, that also means reporting, public disclosure, forms, red tape, etc., you do not need.

Third, Delaware is now regulated by a corporation commission, Nevada is not. You should be aware that any time a state or federal bureaucracy is

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created it immediately begins to make rules and regulations to promote, enlarge, and enhance itself and make itself indispensable and necessary at your expense and inconvenience. No, you don't need added regulation.

Fourth, Delaware, like every one of the other states except Nevada, reports tax data to the Internal Revenue Service.

Fifth, some states make a major item out of the fact they recognize S-Corporations. The status of a corporation as an S-Corporation really has no significance to the corporate owners if the state has no income tax. In Nevada, whether you have an S-Corporation or not really doesn't matter to the Department of Taxation since allocation of taxable income from corporations to the individual has no effect on the state's revenue. Delaware, however, does recognize S-Corporations and therein lies the rub. A Corporation can get S-Corporation treatment to the extent its owners are residents. If there are shareholders who are not Delaware residents, the corporation is taxed on the level of that non-resident ownership. But that's not all, consider these other points:

First, in Delaware you must disclose the date appointed for the next annual meeting of stockholders for election of Directors. You do not have to divulge any information like this in your Nevada corporation.

Second, in Delaware you must disclose in your annual report the location of principal places of business outside of Delaware, this is not required in Nevada.

Third, in Delaware you must list the number and value of shares of stock actually issued. This could be dangerous to you and it is not required in Nevada.

Fourth, in Delaware you must report the transfer of stock, not so in Nevada where maximum flexibility is always maintained.

Fifth, the annual cost to maintain your corporation with 20 million common and 5 million preferred shares as active in Nevada is the modest sum of \$85. This is the fee for filing your annual list of officers and designation of registered agent. For a similar Delaware corporation, the annual fee is more than \$200.

Sixth, in Delaware you must pay tax on income earned in Delaware. The state of Nevada has no income tax either on the corporate or individual level. In fact, Nevada's constitution prohibits personal income tax. In Nevada none of these problems apply, you're free from the regulating hassles which afflict corporations in Delaware.

Clearly the best place to incorporate is Nevada, the state of the future, the frontier state with new horizons. The smart move is to keep in step with progress, to turn from the old to the new. The state of Nevada offers maximum flexibility, maximum privacy, and a minimum of regulation and red tape. As thousands of companies have taken advantage of these opportunities, you too can gain the benefits of incorporating in Nevada. When you do incorporate in Nevada you will find that you have a corporation which will allow you to accomplish all of your goals and all of your objectives.

Let Summit and its partners incorporate for you or purchase our *going public contract* and it is part of the agreement that we will accomplish for you.

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Direct Public Offerings (DPO)

A "Direct Public Offering" (DPO) is a creative form of financing that is just beginning to be used by entrepreneurs nationwide.

This is a stock offering but one that differs considerably from the well known IPO (initial public offering) or venture capital or other forms of early stage financing. It combines elements of these techniques but adds a dimension that can be very powerful for you. DPOs are often used to secure clients, employees, suppliers or distributors as an added arm for your success while giving you the cash you need to grow. DPOs are registered security offerings with state security administrators. They involve simpler procedures and far less cost than a full registration with the SEC. Essentially, they allow small business equal access to the capital markets that are enjoyed by their big corporate brothers and sisters.

Conventional thinking in terms of business development, in financing, or in marketing, all pay very poor dividends today. Competition is just too tough. The use of a DPO can be the novel approach that gives you the capital you need while simultaneously marketing your product or services. A restaurant that sells stock to its customers is an example of a DPO. A smaller bank that has depositors and borrowers alike that own stock is often a DPO. When people are involved with you economically, an "affinity group," they become your loyal and helping supporters. DPOs have been used successfully for pure start-ups as well as firms that had existed and been privately financed for decades.

Over the last 15 years, Fortune 500 companies have reduced their workforce from 16 million to five million. Over the same time period, small business has added 20 million new jobs. They have done that with less than 1% of publicly traded equity capital, It is obvious that if

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this creative force had the money, they could propel the economy forward in spectacular fashion. The SEC has developed a hands-off approach for much of small business stock offerings, preferring that regulatory responsibility be principally with the states. As more people learn about and successfully use a DPO, this type of financing could become a favorite for emerging, high-growth American businesses.

DPOs generally fall under three regulatory classifications, Regulation D Section 504 of the Securities Act of 1933 has become the most widely known, called the "Small Corporate Offering Registration" or "SCOR." SCOR allows you to raise up to \$1 million every twelve months, by registration with state securities administrations. Next, a Regulation A offering extends that size to \$5 million, but also requires a registration with the Small Business Office of the SEC. Finally, intrastate offerings typically have no ceiling. Variations of these three exist as well with even more legal choices, but you'll generally find your needs filled with one of these options. Your attorney or possibly the office of your state security commission can point out advantages and disadvantages, and a free booklet is available from the SEC.

The advantages of doing a DPO versus other types of financing include:

- By selling stock, raising equity, you have capital that you never have to pay back, such as a loan. Also, you don't have the continual need to meet interest and principal payments, or worry that a loan may be called back in,
- Typically, you'll surrender a smaller portion of equity for the same amount of capital than required by venture capitalists or even private placements. The difference lies in the stock market, where valuations are usually far higher than in non-public transactions.
- Undergoing this process gives you the experience with investment banking and shareholders long before you conduct an IPO. You'll know just what your stock can sell for and avoid much of the guesswork that goes into marketing a security.
- DPO sales involve extensive publicity campaigns unlike any other financing. This is a perfect opportunity for potential customers to find out about your company and its products. Money used in selling the stock does double-duty, it simultaneously extends your marketing.
- You can typically "test the waters" by making preliminary inquiries and advertising a potential

stock sale. You can find out a lot before going through the expense and effort of a full-blown effort.

- The involvement of employees, suppliers, distributors and customers with your company all becomes more intensive and lasting when these people are economically motivated to see you succeed. Help can come in so many unexpected ways when you decide to open your vision and some of your profits to others.
- Equity capital can be magic for opening other financing doors and leveraging your company for years to come, Bank loans can be made on a secure basis when the risk has already been thrown off to investors who can sustain it. Government grants and loans, bond offerings, and even venture capital can be more attainable if you've reduced the risk of investing with you.
- By going these extra steps, both you and your company become seasoned prospects and can take a product or service more extensively into a market. By demonstrating that your stock can be sold and your company has a growing market presence, you show the management characteristics that investment money is looking for.
- By successfully becoming a publicly-held company, you'll have a formula for future financing and even new companies. One successful entrepreneur using a DPO has financed more than a dozen.

With every set of advantages, an equal and opposite set of disadvantages exist as well. DPOs are a lot of hard work, getting a document through state regulators or the SEC is no easy task, and the successful sale of your stock can hardly be presumed. So far, most DPOs have been unsuccessful in achieving all their objectives, and this should be a caution to you. Don't let this fact stop you from fully considering a DPO as your best funding method, but don't write off more conventional methods as well. You may find that a DPO is only one part of a variety of financing techniques that properly fit your own growth cycle at different times.

Millions of dollars have been raised in some DPOs with the investment of just a few thousand dollars. Other entrepreneurs have put in hundreds of thousands and come up with nothing. On the surface this looks like a pure gamble, but it doesn't have to be. Enough experience exists to lay out a template for your success, given that you have a company that really warrants investment.

First, you want to have a company and a stock you're really proud of. Does it pass the mother test? Would you want your own mother to buy stock in the company? Now? At this price?

Second, you're asking people who may be friends and neighbors to risk their capital with you. Are you far enough along so they aren't taking unnecessary product development risks that you really should be taking instead?

Third, everything costs money and takes time, usually more than you expected. Are you ready to commit capital and effort to an extensive and complex process that involves a lot of different skills? A DPO runs from soup to nuts, a highly involved document that requires accounting, legal, and business planning skills all the way to marketing and selling stock.

Fourth, can you identify or develop an affinity group who can naturally understand your business and place capital with you? If you haven't figured out just how to sell the issue, you probably won't get it sold.

If you can answer "yes" to all the above, then you're ready to take the first steps to a DPO. These moves should involve more than just yourself. Bring your accountant and your attorney together and lay out what you plan and get their input. They will be intimately involved with your success, and you want them on your side all the way. Next, talk it over with your employees, suppliers and distributors as well. Chances are that you'll get some very good ideas that didn't occur to you before. Contact some investment bankers and ask if they'd be interested in selling your issue. Friends in the media and elsewhere should be informed of your plans since a helpful word dropped by them can prove valuable. Call your state securities commission and ask if they have any suggestions. They may also provide you with a list of some of the companies that have made filings and you could try contacting them to learn of their experience.

The most common form of filing statement for a DPO is known as the "Form U-7" or a "Form 1-A." This consists of a 50 question form that lays out data that eventually becomes an offering statement, a prospectus. The theory had been that a businessman should be able to answer 50 questions and provide enough information for a person to make an intelligent estimate of the stock's attractiveness. Many of the questions will prove "not applicable" but others will take an enormous amount of work and thought. You should not underestimate just how much effort will really go into this. In addition, you'll have filing fees to pay, and eventually a printing bill for the prospectus. Not all the states use the U-7, but all have some variation of the form or an alternative for filing. Experience can be

vastly different, from state to state.

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OTC Bulletin Board

The OTC Bulletin Board[®] (OTCBB) is a regulated quotation service that displays real-time quotes, last-sale prices, and volume information in over-the-counter (OTC) equity securities. An OTC equity security generally is any equity that is not listed or traded on Nasdaq[®] or a national securities exchange. OTCBB securities include national, regional, and foreign equity issues, warrants, units, American Depositary Receipts (ADRs), and Direct Participation Programs (DPPs).

History

In June 1990, the OTCBB began operation, on a pilot basis, as part of important market structure reforms to provide transparency in the OTC equities market. The Penny Stock Reform Act of 1990 mandated the U.S. Securities and Exchange Commission (SEC) to establish an electronic system that met the requirements of Section 17B of the Exchange Act. The system was designed to facilitate the widespread publication of quotation and last-sale information. Since December 1993, firms have been required to report trades in all domestic OTC equity securities through the Automated Confirmation Transaction ServiceSM(ACTSM) within 90 seconds of the transaction.

In April 1997, the SEC approved the operation of the OTCBB on a permanent basis with some modifications, and in May 1997, DPPs became eligible for quotation on the OTCBB. In April 1998, all foreign securities and ADRs that are fully registered with the SEC became eligible for the display of real-time quotes, last-sale prices, and volume information on the OTCBB.

On January 4, 1999, the SEC approved the OTCBB Eligibility Rule. Securities not quoted on the OTCBB as of that date will be required to report their current

financial information to the SEC, banking, or insurance regulators in order to meet eligibility requirements. Non-reporting companies whose securities were already quoted on the OTCBB will be granted a grace period to comply with the new requirements. Those companies will be phased in beginning in July 1999 and by June 2000, current financial information about all domestic companies that are quoted on the OTCBB will be publicly available.

Features

The OTCBB:

- provides access to more than 6,500 securities;
- includes more than 400 participating Market Makers;
- electronically transmits real-time quote, price, and volume information in domestic securities, foreign securities and ADRs; and
- displays indications of interest and prior-day trading activity in DPPs.

Comparison of Nasdaq and OTCBB*

The OTCBB is a quotation medium for subscribing members, not an issuer listing service, and should not be confused with The Nasdaq Stock MarketSM. OTCBB securities are traded by a community of Market Makers that enter quotes and trade reports through a highly sophisticated, closed computer network, which is accessed through Nasdaq Workstation IITM

- the otcbb is unlike the nasdaq stock market in that it:
does not impose listing standards;
- the otcbb is unlike the nasdaq stock market in that it:
does not provide automated trade executions;
- the otcbb is unlike the nasdaq stock market in that it:
does not maintain relationships with quoted issuers; and
- the otcbb is unlike the nasdaq stock market in that it:
does not have the same obligations for Market Makers.

Feature or Requirement	OTCBB	Nasdaq
Minimum quantitative listing requirements	No	Yes
Listing and maintenance fees to issuers	No	Yes
Requirements to maintain quotation or listing	Yes**	Yes

Real-time electronic quotes for domestic issues	Yes	Yes
Minimum Form 211 or listing processing time	3 days	6-8 weeks***

* The OTCBB is separate and distinct from The Nasdaq Stock Market.

** Issuers of securities which began quotation on the OTCBB after January 4, 1999 are required to file periodic financial information with the SEC or other regulatory authority to maintain quotation eligibility.

*** A Form 211 is not required for listing on Nasdaq; however, the average time of approval for listing on Nasdaq is 6-8 weeks.

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The OTCBB is distinct from the Pink Sheets. The "Pink Sheets"® are operated by the National Quotation Bureau, LLC (NQB) and are a static paper quotation medium printed weekly and distributed to broker/dealers. An electronic version of the Pink Sheets is updated once a day and disseminated over market data vendor terminals. The Pink Sheets are not owned or operated by The Nasdaq Stock Market, Inc.

Market Data Dissemination

The following OTCBB data is disseminated through **market data vendor** terminals and Web sites for display to customers worldwide:

- dynamic last-sale and volume information for domestic securities, foreign securities and ADRs;
- end-of-day high, low, close, and volume on DPPs;
- bids, offers, and indications of interest displayed by specific Market Makers;
- inside quotes for domestic securities, foreign securities and ADRs when available;
- indicative quotes for DPPs; and
- Market Makers' telephone numbers.

In addition, all Nasdaq Workstation II subscribers (order-entry firms and Market Makers) may view all OTC Bulletin Board information on their workstations without incurring additional charges.

Market Maker Benefits

Participating Market Makers may:

- register in as many securities as desired;
- update bid and ask quotations on a real-time basis for domestic securities, foreign securities and ADRs and make twice daily quote updates for DPPs;

- enter one-sided or two-sided quotes;
- attract bids through "offer-wanted" (OW) entries and offers through "bid-wanted" (BW) entries; and
- advertise an unsolicited interest in a particular security without specifying a price.

Registering to Make Markets in OTCBB Securities

The OTCBB operates as a dealer system. As a result, all securities being quoted on the OTCBB must be sponsored by a participating Market Maker that registers the security by completing a **Form 211** unless an exemption applies. The Market Maker must submit a Form 211 to the NASD OTC Compliance Unit along with two copies of the required issuer information no less than three business days prior to publication of a quote on the OTC Bulletin Board. Once cleared, Nasdaq Market Data Integrity will notify the Market Maker that it has been registered in the security and may enter a quote.

Ineligible Securities

Every OTC security not currently quoted on the OTC Bulletin Board is considered "ineligible" until a Market Maker submits a **Form 211** or a 15c2-11 Exemption Form. After clearance, the security is granted "eligible" status.

Eligible Securities

If a security has eligible status, it means one or more Market Makers has received clearance to quote the issue on the OTC Bulletin Board within the last 30 days. Any other participating Market Maker that wishes to quote the issue must also submit a completed **Form 211**. During the "eligible" period, a frequency-of-quotation test is administered. The test is described below. Until the test is satisfied, all Market Makers must continue to submit a completed Form 211.

Active Securities

An OTCBB-eligible security that meets the frequency-of-quotation requirement for the so-called "**piggyback**" **exception** is identified in the service as "active." The frequency-of-quotation test or "piggyback" exception is based on whether a broker/dealer has itself published quotations in the security in the applicable interdealer quotation system on at least 12 business days during the preceding 30 calendar days, with not more than four consecutive business days without quotations. Once this criteria has been satisfied, authorized participants may register on-line in a security. As long as the security remains in an "active" state, any participant may quote the security without a Form 211 submission.

Quotation Regulations

The OTC Bulletin Board is monitored by an on-line market surveillance system to help ensure compliance with the existing rules of the SEC and the National Association of Securities Dealers, Inc. (NASD®). Unless there is an exemption, participating Market Makers must comply with the requirements of SEC Rule 15c2-11 on a security-by-security basis to be eligible to quote on the OTCBB.

Reporting Requirements

Market Makers

All trades in domestic equity issues, Canadian issues and ADRs must be reported within 90 seconds through ACT. All other trades may be reported T+1. Please refer to NASD *Notice to Members 93-62* and Rule 6600 for a detailed explanation of the requirements for reporting OTC equity trades.

Issuers

Nasdaq has no business relationship with the issuers quoted in the OTC Bulletin Board. These companies do not have any filing or reporting requirements with The Nasdaq Stock Market, Inc., or the NASD. However, issuers of securities which begin quotation on the OTCBB after January 4, 1999 are subject to periodic filing requirements with the SEC or other regulatory authority. Limited phone, contact, and address information is available in the **Stock Summaries**, which are accessible from the Market Statistics area of this Web site.

Issuer Information

Only Market Makers can apply to quote securities on this service. Issuers may contact an authorized OTCBB Market Maker for sponsorship of a security on the OTCBB. The OTCBB does not charge issuers a fee for being quoted on the service. NASD Rules prohibit Market Makers from accepting any remuneration in return for quoting issuers' securities on the OTCBB or any similar medium.

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Securities Exchange Commission (SEC)

The primary mission of the U.S. Securities and Exchange Commission (SEC) is to protect investors and maintain the integrity of the securities markets. As more and more first-time investors turn to the markets to help secure their futures, pay for homes, and send children to college, these goals are more compelling than ever.

The world of investing is fascinating, complex, and can be very fruitful. But unlike the banking world, where deposits are guaranteed by the federal government, stocks, bonds and other securities can lose value. There are no guarantees. That's why investing should not be a spectator sport; indeed, the principal way for investors to protect the money they put into the securities markets is to do research and ask questions.

The laws and rules that govern the securities industry in the United States derive from a simple and straightforward concept: all investors, whether large institutions or private individuals, should have access to certain basic facts about an investment prior to buying it. To achieve this, the SEC requires public companies to disclose meaningful financial and other information to the public, which provides a common pool of knowledge for all investors to use to judge for themselves if a company's securities are a good investment. Only through the steady flow of timely, comprehensive and accurate information can people make sound investment decisions.

The SEC also oversees other key participants in the securities world, including stock exchanges, broker-dealers, investment advisors, mutual funds, and public utility holding companies. Here again, the SEC is concerned primarily with promoting disclosure of

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important information, enforcing the securities laws, and protecting investors who interact with these various organizations and individuals.

Crucial to the SEC's effectiveness is its enforcement authority. Each year the SEC brings between 400-500 civil enforcement actions against individuals and companies that break the securities laws. Typical infractions include insider trading, accounting fraud, and providing false or misleading information about securities and the companies that issue them.

Fighting securities fraud, however, requires teamwork. At the heart of effective investor protection is an educated and careful investor. The SEC offers the public a wealth of educational information on its Internet website at www.sec.gov. The website also includes the EDGAR database of disclosure documents that public companies are required to file with the Commission.

Though it is the primary overseer and regulator of the U.S. securities markets, the SEC works closely with many other institutions, including Congress, other federal departments and agencies, the self-regulatory organizations (e.g. the stock exchanges), state securities regulators, and various private sector organizations.

This article is an overview of the SEC's history, responsibilities, activities, organization, and operation. More detailed information about many of these topics is available on the SEC website.

Creation of the SEC

The SEC's foundation was laid in an era that was ripe for reform. Before the Great Crash of 1929, there was little support for federal regulation of the securities markets. This was particularly true during the post-World War I surge of securities activity. Proposals that the federal government require financial disclosure and prevent the fraudulent sale of stock were never seriously pursued.

Tempted by promises of "rags to riches" transformations and easy credit, most investors gave little thought to the dangers inherent in uncontrolled market operation. During the 1920s, approximately 20 million large and small shareholders took advantage of post-war prosperity and set out to make their fortunes in the stock market. It is estimated that of the \$50 billion in new securities offered during this period, half became worthless.

When the stock market crashed in October 1929, the fortunes of countless investors were lost. Banks also

lost great sums of money in the Crash because they had invested heavily in the markets. When people feared their banks might not be able to pay back the money that depositors had in their accounts, a "run" on the banking system caused many bank failures.

With the Crash and ensuing depression, public confidence in the markets plummeted. There was a consensus that for the economy to recover, the public's faith in the capital markets needed to be restored. Congress held hearings to identify the problems and search for solutions.

Based on the findings in these hearings, Congress passed the Securities Act of 1933 and the Securities Exchange Act of 1934. These laws were designed to restore investor confidence in our capital markets by providing more structure and government oversight. The main purposes of these laws can be reduced to two common-sense notions:

- Companies publicly offering securities for investment dollars must tell the public the truth about their businesses, the securities they are selling, and the risks involved in investing.
- People who sell and trade securities - brokers, dealers, and exchanges - must treat investors fairly and honestly, putting investors' interests first.

Frequently Asked Questions about the SEC

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Own Your Own Summit Office

Securities Exchange Commission (SEC) rule changes from last year are beginning to take effect and can seriously affect those companies listed and applying for listing on the NASD's Over-the-Counter Bulletin Board (OTC-BB).

On January 5, 1999, the SEC approved several NASD rule changes, one change now required all domestic companies to be "fully reporting" with the SEC. To be fully reporting, a company must have full disclosure to the public.

This is where EDGAR comes in. A company becomes fully reporting by filing the proper forms with the SEC and submitting them through the filing system known as EDGAR.

EDGAR is the acronym for the "Electric Data Gathering, Analysis and Retrieval" system. This system has drastically changed the way public companies file reports, securities registrations and other disclosure documents with the SEC.

EDGAR affords full disclosure to investors on all aspects of the company. This disclosure includes but is not limited to fiscal year end and quarterly financial reports, directors and officers compensation and any partnership agreement or contract that the company has entered into. The information EDGAR provides allows investors to make educated decision on stocks being bought and sold.

In order to submit filings to the SEC via the EDGAR system, the SEC issues special codes and passwords. It is necessary to understand the primary purpose of fully reporting which is full disclosure. Any negative information not disclosed can bring both civil and criminal charges.

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Summit provides many services associated with a EDGAR filing. The company will prepare and write SEC filings, provide printed version for proofing and approval, convert the approved document to comply with the SEC's EDGAR format, create the header data, run validation program prior to submission, transmit filing to SEC, notify upon successful transmission and maintain strict confidentiality prior to public dissemination on the EDGAR system.

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Frequently Asked Questions

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**Frequently Asked Questions of the
SEC**

(Click the question to find the answer)

- I. What Are the Federal Securities Laws?
- II. How Can I Get Answers to My Questions?
- III. Should My Company "Go Public"?
- IV. How Does My Small Business Register a Public Offering?
- V. If My Company Becomes Public, What Disclosures Must I Regularly Make?
- VI. Are there legal ways to offer and Sell Securities Without Registering With the SEC?
 - A. Intrastate Offering Exemption
 - B. Private Offering Exemption
 - C. Regulation A
 - D. Regulation D
 - E. Accredited Investor Exemption - Section 4(6)
 - F. California Small Cap Exemption - Rule 1001
 - G. Exemption for sales of securities through employee benefit plans - Rule 701
- VII. Are There State Law Requirements in Addition to Federal Ones?
- VIII. What Resources Are Available Through the U.S. Small Business Administration?
- IX. Where Can I Go for More Information?

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I. What Are the Federal Securities Laws?

In the chaotic securities markets of the 1920s, companies often sold stocks and bonds on the basis of glittering promises of fantastic profits - without disclosing any meaningful information to investors. These conditions contributed to the disastrous Stock Market Crash of 1929. In response, the U.S. Congress enacted the federal securities laws and created the Securities and Exchange Commission (SEC) to administer them.

There are two primary sets of federal laws that come into play when a company wants to offer and sell its securities to the public. They are:

- the Securities Act of 1933 (Securities Act), and
- the Securities Exchange Act of 1934 (Exchange Act).

Securities Act

The Securities Act generally requires companies to give investors "full disclosure" of all "material facts," the facts investors would find important in making an investment decision. This Act also requires companies to file a registration statement with the SEC that includes information for investors. The SEC does not evaluate the merits of offerings, or determine if the securities offered are "good" investments. The SEC staff reviews registration statements and declares them "effective" if companies satisfy our disclosure rules. We describe this process in more detail beginning on page 7.

Exchange Act

The Exchange Act requires publicly held companies to disclose information continually about their business operations, financial conditions, and managements. These companies, and in many cases their officers, directors and significant shareholders, must file periodic reports or other disclosure documents with the SEC. In some cases, the company must deliver the information directly to investors. We discuss these obligations more fully beginning on page 11.

Exemptions

Your company may be exempt from these registration and reporting requirements. We discuss exemptions beginning on page 16.

Beginning of FAQ SEC

II. How Can I Get Answers to My Questions?

The SEC tries to meet the needs of small business through its rules and regulations. It also offers informal guidance by answering your questions over the phone, through the mail or by e-mail. The SEC offers you a number of ways to express your views and get help from the staff. Of course, you should always retain competent counsel before engaging in any securities offering.

Special Ombudsman to Serve You

In 1996, we appointed a Special Ombudsman for Small Business to serve you and to represent the concerns of smaller companies within the SEC. You can tell the Ombudsman your concerns about any SEC proposal or rule. The Ombudsman also can answer your general questions or help you find the answers to your specific questions. The Ombudsman's telephone number is (202) 942-2950.

The Office of Small Business

The Division of Corporation Finance's Office of Small Business directs the SEC's small business rulemaking initiatives and comments on SEC rule proposals affecting small companies. Its staff works with Congressional committees, government agencies, and other groups concerned with small business. The Office also specializes in the review of filings from small companies. Its telephone number is (202) 942-2950.

Town Hall Meetings

The Office of Small Business also sponsors small business town hall meetings across the country. These meetings help the SEC convey basic information to small businesses and learn more about the problems small businesses face in raising capital. These meetings help the SEC design programs that meet small businesses' needs while protecting investors.

Government-Business Forum on Small Business Capital Formation

In addition to the town hall meetings, the SEC sponsors the Government-Business Forum on Small Business Capital Formation. This annual meeting provides the only national forum for small businesses to let government officials from different parts of the federal government know how the laws, rules and regulations impact the ability of small companies to raise capital. You can get more information about this forum from the Office of Small Business.

Internet Web Site

We also maintain a home page on the World Wide Web at <http://www.sec.gov/>. Our site includes recent SEC releases and other updating information of interest to small companies. Through our Web site, small companies and investors can also find documents publicly filed on the SEC's Electronic Data Gathering, Analysis, and Retrieval, or EDGAR, system. Most registration statements and other documents must now be filed electronically via that system.

Beginning of FAQ SEC

III. Should My Company "Go Public"?

When your company needs additional capital, "going public" may be the right choice, but you should weigh your options carefully. If your company is in the very early stages of development, it may be better to seek loans from financial institutions or the Small Business Administration. Other alternatives include raising money by selling securities in transactions that are exempt from the registration process. We discuss these alternatives later.

There are benefits and new obligations that come from raising capital through a public offering registered with the SEC. While the benefits are attractive, be sure you are ready to assume these new obligations:

Benefits

- Your access to capital will increase, since you can contact more potential investors.
- Your company may become more widely known.
- You may obtain financing more easily in the future if investor interest in your company grows enough to sustain a secondary trading market in your securities.
- Controlling shareholders, such as the company's officers or directors, may have a ready market for their shares, which means that they can more easily sell their interests at retirement, for diversification, or for some other reason.
- Your company may be able to attract and retain more highly qualified personnel if it can offer stock options, bonuses, or other incentives with a known market value.
- The image of your company may be improved.

New Obligations

- You must continue to keep shareholders informed about the company's business operations, financial condition, and management, incurring additional costs and new legal obligations.
- You may be liable if you do not fulfill these new legal obligations.
- You may lose some flexibility in managing your company's affairs, particularly when shareholders must approve your actions.
- Your public offering will take time and money to accomplish.

Beginning of FAQ SEC

IV. How Does My Small Business Register a Public Offering?

If you decide on a registered public offering, the Securities Act requires your company to file a registration statement with the SEC before the company can offer its securities for sale. You cannot actually sell the securities covered by the registration statement until the SEC staff declares it "effective," even though registration statements become public immediately upon filing.

Registration statements have two principal parts:

- Part I is the prospectus, the legal offering or "selling" document. Your company - the "issuer" of the securities - must describe in the prospectus the important facts about its business operations, financial condition, and management. Everyone who buys the new issue, as well as anyone who is made an offer to purchase the securities, must have access to the prospectus.
- Part II contains additional information that the company does not have to deliver to investors. Anyone can see this information by requesting it from one of the SEC's public reference rooms or by looking it up on the SEC Web site.

The Basic Registration Form - Form S-1

All companies can use Form S-1 to register their securities offerings. You should not prepare a registration statement as a fill-in-the-blank form, like a tax return. It should be similar to a brochure, providing readable information. If you file this form, your company must describe each of the following in the prospectus:

- its business;
- its properties;
- its competition;
- the identity of its officers and directors and their compensation;
- material transactions between the company and its officers and directors;
- material legal proceedings involving the company or its officers and directors;
- the plan for distributing the securities; and the intended use of the proceeds of the offering.

Information about how to describe these items is set out in SEC rules. Registration statements also must include financial statements audited by an independent certified public accountant.

In addition to the information expressly required by the form, your company must also provide any other information that is necessary to make your disclosure complete and not misleading. You also must clearly describe any risks prominently in the prospectus, usually at the beginning. Examples of these risk factors are:

- lack of business operating history;
- adverse economic conditions in a particular industry;
- lack of a market for the securities offered; and
- dependence upon key personnel.

Alternative Registration Forms for Small Business Issuers

If your company qualifies as a "small business issuer," it can choose to file its registration statement using one of the simplified small business forms. A small business issuer is a United States or Canadian issuer:

- that had less than \$25 million in revenues in its last fiscal year, and
- whose outstanding publicly-held stock is worth no more than \$25 million.

Form SB-1 - To Raise \$10 Million or Less

Small business issuers offering up to \$10 million worth of securities in any 12-month period may use Form SB1. This form allows you to provide information in a question and answer format, similar to that used in Regulation A offerings, a type of exempt offering discussed on page 19. Unlike Regulation A filings, Form SB-1 requires audited financial statements.

Form SB-2 - To Raise Capital in Any Amount

If your company is a "small business issuer," it may register an unlimited dollar amount of securities using Form SB-2, and may use this form again and again so long as it satisfies the "small business issuer" definition.

One advantage of Form SB-2 is that all its disclosure requirements are in Regulation S-B, a set of rules written in simple, non-legalistic terminology. Form SB-2 also permits the company to:

- Provide audited financial statements, prepared according to generally accepted accounting principles, for two fiscal years. In contrast, Form S-1 requires the issuer to provide audited financial statements, prepared according to more detailed SEC regulations, for three fiscal years; and
- Include less extensive narrative disclosure than Form S-1 requires, particularly in the description of your business, and executive compensation.

Staff Review of Registration Statements

SEC staff examines registration statements for compliance with disclosure requirements. If a filing appears incomplete or inaccurate, the staff usually informs the company by letter. The company may file correcting or clarifying amendments. Once the company has satisfied the disclosure requirements, the staff declares the registration statement effective. The company may then begin to sell its securities. The SEC can refuse or suspend the effectiveness of any registration statement if it concludes that the document is misleading, inaccurate, or incomplete.

Beginning of FAQ SEC

V. If My Company Becomes Public, What Disclosures Must I Regularly Make?

Your company can become "public" in one of two ways - by issuing securities in an offering registered under the Securities Act or by registering the company's outstanding securities under Exchange Act requirements. Both types of registration trigger ongoing reporting obligations for your company. In some cases, the Exchange Act also subjects your company's officers, directors and significant shareholders to reporting requirements. Let's discuss these requirements individually.

Reporting obligations because of Securities Act registration

Once the staff declares your company's Securities Act registration statement effective, the Exchange Act requires you to file reports with the SEC. The obligation to file reports continues at least through the end of the fiscal year in which your registration statement becomes effective. After that, you are required to continue reporting unless you satisfy the following "thresholds," in which case your filing obligations are suspended:

- your company has fewer than 300 shareholders of the class of securities offered; or
- your company has fewer than 500 shareholders of the class of securities offered and less than \$10 million in total assets for each of its last three fiscal years.

If your company is subject to the reporting requirements, it must file information with the SEC about:

- its operations;
- its officers, directors, and certain shareholders, including salary, various fringe benefits, and transactions between the company and management;
- the financial condition of the business, including financial statements audited by an independent certified public accountant; and
- its competitive position and material terms of contracts or lease agreements.

All of this information becomes publicly available when you file your reports with the SEC. As is true with Securities Act filings, small business issuers may choose to use small business alternative forms and Regulation S-B for registration and reporting under the Exchange Act.

Obligations because of Exchange Act registration

Even if your company has not registered a securities offering, it must file an Exchange Act registration statement if:

- it has more than \$10 million total assets and a class of equity securities, like common stock, with 500 or more shareholders; or
- it lists its securities on an exchange or on Nasdaq.

If a class of your company's securities is registered under the Exchange Act, the company, as well as its shareholders and management, are subject to various reporting requirements, explained below.

Ongoing Exchange Act periodic reporting

If your company registers a class of securities under the Exchange Act, it must file the same annual, periodic, and current reports that are required as a result of Securities Act registration, as explained above. This obligation continues for as long as the company exceeds the reporting thresholds previously outlined on page 11. If your company's securities are traded on an exchange or on Nasdaq, the company must continue filing these reports as long as the securities trade on those markets, even if your company falls below the thresholds.

Proxy rules

A company with Exchange Act registered securities must comply with the SEC's proxy rules whenever it seeks a shareholder vote on corporate matters. These rules require the company to provide a proxy statement to its shareholders, together with a proxy card when soliciting proxies. Proxy statements discuss management and executive compensation, along with descriptions of the matters up for a vote. If the company is not soliciting proxies but will take a vote on a matter, the company must provide to its shareholders an information statement that is similar to a proxy statement. The proxy rules also require your company to send an annual report to shareholders if there will be an election of directors. These reports contain much of the same information found in the Exchange Act annual reports that a company must file with the SEC, including audited financial statements. The proxy rules also govern when your company must provide shareholder lists to investors and when it must include a shareholder proposal in the proxy statement.

Beneficial ownership reports

If your company has registered a class of its equity securities under the Exchange Act, persons who acquire more than five percent of the outstanding shares of that class must file beneficial owner reports until their holdings drop below five percent. These filings contain background information about the beneficial owners as well as their investment intentions, providing investors and the company with information about accumulations of securities that may potentially change or influence company management and policies.

Tender offers

A public company with Exchange Act registered securities that faces a takeover attempt, or third party tender offer, should be aware that the SEC's tender offer rules will apply to the transaction. The same is true if the company makes a tender offer for its own Exchange Act registered securities. The filings required by these rules provide information to the public about the person making the tender offer. The company that is the subject of the takeover must file with the SEC its responses to the tender offer. The rules also set time limits for the tender offer and provide other protections to shareholders.

Transaction reporting by officers, directors and ten percent shareholders

Section 16 of the Exchange Act applies to your company's directors and officers, as well as shareholders who own more than 10% of a class of your company's equity securities registered under the Exchange Act. It requires these persons to report their transactions involving the company's equity securities to the SEC. Section 16 also establishes mechanisms for a company to recover "short swing" profits, those profits an insider realizes from a purchase and sale of a company security within a six-month period. In addition, Section 16 prohibits short selling by these persons of any class of the company's securities, whether or not that class is registered under the Exchange Act.

Begining of FAQ SEC

VI. Are There Legal Ways To Offer and Sell Securities Without Registering With the SEC?

Yes! Your company's securities offering may qualify for one of several exemptions from the registration requirements. We explain the most common ones below. You must remember, however, that all securities transactions, even exempt transactions, are subject to the antifraud provisions of the federal securities laws. This means that you and your company will be responsible for false or misleading statements, whether oral or written. The government enforces the federal securities laws through criminal, civil and administrative proceedings. Some enforcement proceedings are brought through private law suits. Also, if all conditions of the exemptions are not met, purchasers may be able to obtain refunds of their purchase price. In addition, offerings that are exempt from provisions of the federal securities laws may still be subject to the notice and filing obligations of various state laws. Make sure you check with the appropriate state securities administrator before proceeding with your offering.

A. Intrastate Offering Exemption

Section 3(a)(11) of the Securities Act is generally known as the "intrastate offering exemption." This exemption facilitates the financing of local business operations. To qualify for the intrastate offering exemption, your company must:

- be incorporated in the state where it is offering the securities;
- carry out a significant amount of its business in that state; and
- make offers and sales only to residents of that state.

There is no fixed limit on the size of the offering or the number of purchasers. Your company must determine the residence of each purchaser. If any of the securities are offered or sold to even one out-of-state person, the exemption may be lost. Without the exemption, the company could be in violation of the Securities Act registration requirements. If a purchaser resells any of the securities to a person who resides outside the state within a short period of time after the company's offering is complete (the usual test is nine months), the entire transaction, including the original sales, might violate the Securities Act. Since secondary markets for these securities rarely develop, companies often must sell securities in these offerings at a discount.

It will be difficult for your company to rely on the intrastate exemption unless you know the purchasers and the sale is directly negotiated with them. If your company holds some of its assets outside the state, or derives a substantial portion of its revenues outside the state where it proposes to offer its securities, it will probably have a difficult time qualifying for the exemption.

You may follow Rule 147, a "safe harbor" rule, to ensure that you meet the requirements for this exemption. It is possible, however, that transactions not meeting all requirements of Rule 147 may still qualify for the exemption.

B. Private Offering Exemption

Section 4(2) of the Securities Act exempts from registration "transactions by an issuer not involving any public offering." To qualify for this exemption, the purchasers of the securities must:

- have enough knowledge and experience in finance and business matters to evaluate the risks and merits of the investment (the "sophisticated investor"), or be able to bear the

- investment's economic risk;
- have access to the type of information normally provided in a prospectus; and
- agree not to resell or distribute the securities to the public.

In addition, you may not use any form of public solicitation or general advertising in connection with the offering.

The precise limits of this private offering exemption are uncertain. As the number of purchasers increases and their relationship to the company and its management becomes more remote, it is more difficult to show that the transaction qualifies for the exemption. You should know that if you offer securities to even one person who does not meet the necessary conditions, the entire offering may be in violation of the Securities Act.

Rule 506, another "safe harbor" rule, provides objective standards that you can rely on to meet the requirements of this exemption. Rule 506 is a part of Regulation D, which we describe more fully on page 24.

C. Regulation A

Section 3(b) of the Securities Act authorizes the SEC to exempt from registration small securities offerings. By this authority, we created Regulation A, an exemption for public offerings not exceeding \$5 million in any 12-month period. If you choose to rely on this exemption, your company must file an offering statement, consisting of a notification, offering circular, and exhibits, with the SEC for review.

Regulation A offerings share many characteristics with registered offerings. For example, you must provide purchasers with an offering circular that is similar in content to a prospectus. Like registered offerings, the securities can be offered publicly and are not "restricted," meaning they are freely tradeable in the secondary market after the offering. The principal advantages of Regulation A offerings, as opposed to full registration, are:

- The financial statements are simpler and don't need to be audited;
- There are no Exchange Act reporting obligations after the offering unless the company has more than \$10 million in total assets and more than 500 shareholders;
- Companies may choose among three formats to prepare the offering circular, one of which is a simplified question-and-answer document; and

- You may "test the waters" to determine if there is adequate interest in your securities before going through the expense of filing with the SEC.

All types of companies which do not report under the Exchange Act may use Regulation A, except "blank check" companies, those with an unspecified business, and investment companies registered or required to be registered under the Investment Company Act of 1940. In most cases, shareholders may use Regulation A to resell up to \$1.5 million of securities.

If you "test the waters," you can use general solicitation and advertising prior to filing an offering statement with the SEC, giving you the advantage of determining whether there is enough market interest in your securities *before* you incur the full range of legal, accounting, and other costs associated with filing an offering statement. You may not, however, solicit or accept money until the SEC staff completes its review of the filed offering statement and you deliver prescribed offering materials to investors.

D. Regulation D

Regulation D establishes three exemptions from Securities Act registration. Let's address each one separately.

Rule 504

Rule 504 provides an exemption for the offer and sale of up to \$1,000,000 of securities in a 12-month period. Your company may use this exemption so long as it is not a blank check company and is not subject to Exchange Act reporting requirements. Like the other Regulation D exemptions, in general you may not use public solicitation or advertising to market the securities and purchasers receive "restricted" securities, meaning that they may not sell the securities without registration or an applicable exemption. However, you can use this exemption for a public offering of your securities and investors will receive freely tradable securities under the following circumstances:

- You register the offering exclusively in one or more states that require a publicly filed registration statement and delivery of a substantive disclosure document to investors;
- You register and sell in a state that requires registration and disclosure delivery and also sell in a state without those requirements, so long as you deliver the disclosure documents mandated by the state in which you registered to all purchasers; or,

- You sell exclusively according to state law exemptions that permit general solicitation and advertising, so long as you sell only to "accredited investors," a term we describe in more detail below in connection with Rule 505 and Rule 506 offerings.

Even if you make a private sale where there are no specific disclosure delivery requirements, you should take care to provide sufficient information to investors to avoid violating the antifraud provisions of the securities laws. This means that any information you provide to investors must be free from false or misleading statements. Similarly, you should not exclude any information if the omission makes what you do provide investors false or misleading.

Rule 505

Rule 505 provides an exemption for offers and sales of securities totaling up to \$5 million in any 12-month period. Under this exemption, you may sell to an unlimited number of "accredited investors" and up to 35 other persons who do not need to satisfy the sophistication or wealth standards associated with other exemptions. Purchasers must buy for investment only, and not for resale. The issued securities are "restricted." Consequently, you must inform investors that they may not sell for at least a year without registering the transaction. You may not use general solicitation or advertising to sell the securities.

An "accredited investor" is:

- a bank, insurance company, registered investment company, business development company, or small business investment company;
- an employee benefit plan, within the meaning of the Employee Retirement Income Security Act, if a bank, insurance company, or registered investment adviser makes the investment decisions, or if the plan has total assets in excess of \$5 million;
- a charitable organization, corporation or partnership with assets exceeding \$5 million;
- a director, executive officer, or general partner of the company selling the securities;
- a business in which all the equity owners are accredited investors;
- a natural person with a net worth of at least \$1 million;
- a natural person with income exceeding \$200,000 in each of the two most recent years or joint income with a spouse exceeding

\$300,000 for those years and a reasonable expectation of the same income level in the current year; or

- a trust with assets of at least \$5 million, not formed to acquire the securities offered, and whose purchases are directed by a sophisticated person.

It is up to you to decide what information you give to accredited investors, so long as it does not violate the antifraud prohibitions. But you must give non-accredited investors disclosure documents that generally are the same as those used in registered offerings. If you provide information to accredited investors, you must make this information available to the non-accredited investors as well. You must also be available to answer questions by prospective purchasers.

Here are some specifics about the financial statement requirements applicable to this type of offering:

- Financial statements need to be certified by an independent public accountant;
- If a company other than a limited partnership cannot obtain audited financial statements without unreasonable effort or expense, only the company's balance sheet, to be dated within 120 days of the start of the offering, must be audited; and
- Limited partnerships unable to obtain required financial statements without unreasonable effort or expense may furnish audited financial statements prepared under the federal income tax laws.

Rule 506

As we discussed earlier, Rule 506 is a "safe harbor" for the private offering exemption. If your company satisfies the following standards, you can be assured that you are within the Section 4(2) exemption:

- You can raise an unlimited amount of capital;
- You cannot use general solicitation or advertising to market the securities;
- You can sell securities to an unlimited number of accredited investors (the same group we identified in the Rule 505 discussion) and up to 35 other purchasers. Unlike Rule 505, all non-accredited investors, either alone or with a purchaser representative, must be sophisticated - that is, they must have sufficient knowledge and experience in financial and business matters to make them capable of

evaluating the merits and risks of the prospective investment;

- It is up to you to decide what information you give to accredited investors, so long as it does not violate the antifraud prohibitions. But you must give non-accredited investors disclosure documents that generally are the same as those used in registered offerings. If you provide information to accredited investors, you must make this information available to the non-accredited investors as well;
- You must be available to answer questions by prospective purchasers;
- Financial statement requirements are the same as for Rule 505; and
- Purchasers receive "restricted" securities. Consequently, purchasers may not freely trade the securities in the secondary market after the offering.

E. Accredited Investor Exemption - Section 4(6)

Section 4(6) of the Securities Act exempts from registration offers and sales of securities to accredited investors when the total offering price is less than \$5 million.

The definition of accredited investors is the same as that used in Regulation D. Like the exemptions in Rule 505 and 506, this exemption does not permit any form of advertising or public solicitation. There are no document delivery requirements. Of course, all transactions are subject to the antifraud provisions of the securities laws.

F. California Small Cap Exemption - Rule 1001

SEC Rule 1001 provides an exemption from the registration requirements of the Securities Act for offers and sales of securities, in amounts of up to \$5 million, that satisfy the conditions of §25102(n) of the California Corporations Code. This California law exempts from California state law registration offerings made by California companies to "qualified purchasers" whose characteristics are similar to, but not the same as, accredited investors under Regulation D. This exemption allows some methods of general solicitation prior to sales.

G. Exemption for Sales of Securities through Employee Benefit Plans - Rule 701

The SEC's Rule 701 exempts sales of securities if made to compensate employees. This exemption is available only to companies that are not subject to Exchange Act reporting requirements. You can sell at

least \$1,000,000 of securities under this exemption, no matter how small your company is. You can sell even more if you satisfy certain formulas based on your company's assets or on the number of its outstanding securities. If you sell more than \$5 million in securities in a 12-month period, you need to provide limited disclosure documents to your employees. Employees receive "restricted securities" in these transactions and may not freely offer or sell them to the public.

Beginning of FAQ SEC

VII. Are There State Law Requirements in Addition to Federal Ones?

The federal government and state governments each have their own securities laws and regulations. If your company is selling securities, it must comply with federal *and* state securities laws. If a particular offering is exempt under the federal securities laws, that does not necessarily mean that it is exempt from any of the state laws.

Historically, most state legislatures have followed one of two approaches in regulating public offerings of securities, or a combination of the two approaches. Some states review small businesses' securities offerings to ensure that companies disclose to investors all information needed to make an informed investment decision. Other states also analyze public offerings using substantive standards to assure that the terms and structure of the offerings are fair to investors, in addition to the focus on disclosure.

To facilitate small business capital formation, the North American Securities Administrators Association, or NASAA, in conjunction with the American Bar Association, developed the Small Company Offering Registration, also known as SCOR. SCOR is a simplified "question and answer" registration form that companies also can use as the disclosure document for investors. SCOR was primarily designed for state registration of small business securities offerings conducted under the SEC's Rule 504, for sale of securities up to \$1,000,000, discussed on page 20. Currently, over 45 states recognize SCOR. To assist small business issuers in completing the SCOR Form, NASAA has developed a detailed "Issuer's Manual." This manual is available through NASAA's Web site at <http://www.sec.gov/cgi-bin/goodbye.cgi?www.nasaa.org>.

In addition, a small company can use the SCOR Form, called Form U-7, to satisfy many of the filing requirements of the SEC's Regulation A exemption, for sales of securities of up to \$5,000,000 (discussed on page 19), since the company may file it with the SEC

as part of the Regulation A offering statement.

To assist small businesses offering in several states, many states coordinate SCOR or Regulation A filings through a program called regional review. Regional reviews are available in the New England, Mid-Atlantic, Midwest and Western regions.

Companies seeking additional information on SCOR, regional reviews or the "Issuer's Manual" should contact NASAA.

Beginning of FAQ SEC

VIII. What Resources Are Available Through the U.S. Small Business Administration?

When assessing your capital needs, you should consider programs offered through the U.S. Small Business Administration (SBA). Congress established the SBA in 1953 to aid, counsel, and protect the interests of the Nation's small business community. The SBA accomplishes this in part by working with intermediaries, banks, and other lending institutions to provide loans and venture capital financing to small businesses unable to secure financing through normal lending channels. The SBA offers financing through the programs listed below.

7(a) Loan Guaranty Program:

This is the SBA's primary lending program and was designed to meet the majority of the small business lending community's financing needs. In addition to general financing, the 7(a) program also encompasses a number of specialized loan programs. The following are a few of the many specialized loan programs:

Low Doc

This program is designed to increase the availability of funds under \$100,000 and streamline or expedite the loan review process.

CAPLines

An umbrella program to help small businesses meet their short-term and cyclical working-capital needs with five separate programs.

International Trade

If your business is preparing to engage in or is already

engaged in international trade, or is adversely affected by competition from imports, the International Trade Loan Program is for you; and

DELTA

Defense Loan and Technical Assistance is a joint SBA and Department of Defense effort to provide financial and technical assistance to defense-dependent small firms adversely affected by cutbacks in defense.

Microloan Program

This program works through intermediaries to provide small loans from as little as \$100 up to \$25,000.

Certified Development Company (504 Loan) Program

This program, commonly referred to as the 504 program, makes long term loans available for purchasing land, buildings, machinery and equipment, and for building, modernizing or renovating existing facilities and sites.

Small Business Investment Company Program

Small Business Investment Companies (SBICs), which the SBA licenses and regulates, are privately-owned and managed investment firms that provide venture capital and start-up financing to small businesses.

To find additional information on these and other financial programs please contact your local SBA District Office (call 1-800-8-ASK-SBA for the nearest office) or look on SBA's Web site (<http://www.sba.gov>).

Additional Financial Resources and Information from the SBA's Office of Advocacy

Angel Capital Electronic Network (ACE-Net)

The Office of Advocacy of SBA has established an Internet site where small companies may list their Regulation A and Regulation D 504/SCOR stock offerings. ACE-Net is a cooperative effort between SBA and nine universities, state-based entities, and other non-profit organizations to provide a listing service where small companies may list their stock offering for review by high net worth investors (accredited investors). In addition, ACE-Net anticipates providing mentoring and educational services for small companies needing business planning and securities information. You can find the ACE-Net Internet site at the following URLs: <http://www.sec.gov/cgi-bin/goodbye.cgi?www.sba.gov/ADVO/> or

<http://www.sec.gov/cgi-bin/goodbye.cgi?www.ace-net.org>.

Small Business Lending in the United States

The Office of Advocacy of SBA has ranked the nearly 10,000 banks in the country on a state-by-state basis to determine which banks are "small business friendly." The state-by-state directory helps small businesses locate which banks in their area are more likely to lend to small business. The directory is available over the Internet at: <http://www.sec.gov/cgi-bin/goodbye.cgi?www.sba.gov/ADVO/stats/>.

Beginning of FAQ SEC

IX. Where Can I Go for More Information?

The staff of the SEC's Office of Small Business and the SEC's Small Business Ombudsman will be glad to assist you with any questions you may have regarding federal securities laws. For information about state securities laws, contact NASAA or your state's securities administrator, whose office is usually located in your capital city.

The entire text of the SEC's rules and regulations is available through the U.S. Government Printing Office or from several private publishers of legal information. In addition, numerous books on this subject have been published, and some are available at public libraries. As of this writing, the following volumes of Title 17 of the Code of Federal Regulations (the SEC's rules and regulations) were available from the Government Printing Office:

- Vol. II - Parts 200 to 239. SEC Organization; Conduct and Ethics; Information and Requests; Rules of Practice; Regulation S-X and Securities Act of 1933.
- Vol III - Parts 240 to End. Securities Exchange Act of 1934; Public Utility Holding Company, Trust Indenture, Investment Company, Investment Advisers, and Securities Investor Protection Corporation Acts.

For additional information about how to obtain official publications of Commission rules and regulations, contact:

Superintendent of Documents
Government Printing Office
Washington DC 20402-9325

For copies of SEC forms and recent SEC releases:

Publications Section
U.S. Securities and Exchange Commission
450 Fifth Street N.W.
Washington, D.C. 20549-0019
Telephone: (202)942-4046

Other useful addresses, telephone numbers, Web sites
and e-mail:

SEC's World Wide Web site:
<http://www.sec.gov/>

SEC Office of Small Business
SEC Small Business Ombudsman
U.S. Securities and Exchange Commission
450 Fifth Street, N.W.
Washington, D.C. 20549-0304
Telephone: (202) 942-2950
E-mail addresses:
e-prospectus@sec.gov
help@sec.gov

North American Securities Administrators
Association
10 "G" Street, N.E., Suite 710
Washington, D.C. 20002
(202) 737-0900
NASAA's World Wide Web site:
[http://www.sec.gov/cgi-bin/goodbye.cgi?](http://www.sec.gov/cgi-bin/goodbye.cgi?www.nasaa.org)
www.nasaa.org

SBA's World Wide Web site:
<http://www.sec.gov/cgi-bin/goodbye.cgi?www.sba.gov>

ACE-Net World Wide Web site:
[http://www.sec.gov/cgi-bin/goodbye.cgi?www.ace-](http://www.sec.gov/cgi-bin/goodbye.cgi?www.ace-net.org)
[net.org](http://www.ace-net.org)

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Frequently Asked Questions about DPOs

Is your company asking...

**How do I finance my emerging high growth
business?**

If your business is looking for capital in the \$1 million to
\$20 million area, you should consider a new instrument
promoted by the White House, Federal Reserve Banks

and other organizations that want to see you succeed. Direct Public Offerings (DPOs) are smaller stock offerings that permit you access to capital free from traditional line of credit commitment that can immediately help market your company. A DPO makes you a stock issuer.

I. What is a DPO?

II. Why shouldn't I just borrow from a bank?

III. Could I lose control of my company?

IV. Why shouldn't I do an initial public offering (IPO) with a large investment banker?

V. What types of companies have been successful in doing DPOs?

VI. What if my immediate cash needs aren't that big?

VII. What are the advantages of using a DPO in place of or to complement a private placement memorandum?

VIII. How do I conduct a DPO?

I. What is a DPO?

A registration statement is submitted to the SEC and State Regulatory Commissions and gives you the legal authority to create stock. You can then tap into retirement funds, legally advertise your stock, acquire other companies with a stock swap, form strategic relationships by having others buy into you and a host of other attractive expansion features. The stock sale is conducted by vigorously marketing your company and products and getting the word out about your opportunity to potential investors around the world!

Beginning of FAQ DPOs

II. Why shouldn't I just borrow from a bank?

In many cases you should but consider that banks are in the business of making secured loans against assets and your company growth probably requires permanent capital that can take risks. If you go to your loan officer with an equity base already intact you become a lot more bankable.

Beginning of FAQ DPOs

III. Could I lose control of my company?

A DPO is usually done for a fifth or less of the total outstanding shares so the entrepreneur can maintain ownership easily. Most other financing terms are far less attractive and don't put you in the driver's seat or give you the flexibility of a DPO.

Beginning of FAQ DPOs

IV. Why shouldn't I do an initial public offering (IPO) with a large investment banker?

The typical IPO is for \$23 million and involves a front-end cost of \$500,000 or more. If you're there now, fine, but if not a DPO is a very economical step for you to take first and eventually grow your company to the IPO status.

Beginning of FAQ DPOs

V. What types of companies have been successful in doing DPOs?

High-tech, low-tech, start-ups and mature companies all have used DPOs. Shareholders typically buy 100% to 300% more of a company's products or services than the typical client and DPOs should be considered as a strong marketing tool.

Beginning of FAQ DPOs

VI. What if my immediate cash needs aren't that big?

A DPO is flexible enough to reflect your immediate financing but also to give you a mechanism for more money as you grow. You can control your cash needs and future on your terms.

Beginning of FAQ DPOs

VII. What are the advantages of using a DPO in place of or to complement a private placement memorandum?

- A DPO can be freely advertised and is not limited on the number of subscribers.

- The typical investor qualifications are eliminated (California retains minimal factors).
- An offering comes with the SEC and State Securities Commissions "Seal." (Qualification.)
- Foreign securities agencies usually accept an SEC qualified offering without further problems.
- A DPO offering circular is a readable document with color illustrations and is printed in exactly the same format as an IPO offered by Morgan Stanley or Goldman Sachs.
- Publicity associated with a DPO provides invaluable marketing and development benefits including the possibility of a buy-out, IPO, merger, strategic partner, increased sales, added personnel, added distributors, etc.
- Creating a publicly held security gives the company leverage to use its stock for acquisitions and
- other purposes over and above the money raised.
- Popular forms of registration include Regulation A, allowing the raising of up to \$5 million of capital each twelve months and an SB-2 which allows up to \$10 million.
- The procedure for qualification has been deliberately shortened with SEC comments on the first submission received back in just **30** days. The process will go on from there but need not be lengthy given a well-prepared offering at the beginning.
- Go Public Today can prepare a submission to the SEC **quickly**.
- SEC attorneys and accountants examine the document in detail (without charge) and state just what has to be changed to be in full compliance with the laws and regulations.
- An SEC qualified document is **legally** much more protective of the entrepreneur, underwriter, placement agent, promoter, etc. than a Private Placement Memorandum (PPM).
- A book on DPOs by Drew Field (about \$19.95) illustrates the entire process and gives whole chapters on use of the Internet and numerous examples of companies that have been involved and what did and did not work. (*Price Club* did one for \$71 million; a \$100,000 offering was made in Mississippi).
- A PPM may be far more salable when it is to be quickly followed by a DPO at a public offering price higher than that given in the PPM.
- A private placement or other form of early stage investment is usually **recorded on the books** at cost regardless of how well the company may be growing. A DPO may allow the early stage

investors to record their investment value at the public offering or traded price. (Check this with your own CPA).

Beginning of FAQ DPOs

VIII. How do I conduct a DPO?

Contact Summit for more information.

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Frequently Asked Questions of the OTCBB

I. Can a security be traded on the OTC Bulletin Board® (OTCBB) and Nasdaq® at the same time?

II. What is the difference between the OTC market and a stock exchange?

III. How does the OTCBB differ from the Pink Sheets?

IV. What is an other-OTC security?

V. What are the listing requirements for the OTCBB?

VI. Are there trading halts on OTCBB securities?

VII. What are the quotation increments/minimum quote size for OTCBB securities?

VIII. How do I withdraw from an OTCBB stock?

XIX. How can I get trade and quote data for OTCBB securities?

X. Where can I get historical trade and quote data for OTCBB securities?

XI. How does a company get on the OTCBB?

XII. Are there filing requirements for OTCBB issuers?

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XVI. Why don't I receive Inside Quote information for all OTCBB securities?

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XX. How are symbols assigned?

XXI. Do I have to file a Form 211 for a New York Stock Exchange or American Stock?

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XXIII. Do financials submitted with the Form 211 have to be audited?
XXIV. What is the source of historical OTCBB trading data?
-

I. Can a security be traded on the OTC Bulletin Board® (OTCBB) and Nasdaq® at the same time?

No. The OTCBB is a quotation service for securities which are not listed or traded on Nasdaq or a national securities exchange. It is possible, however, for a security to list or delist from Nasdaq intraday, and therefore move from the OTCBB to Nasdaq or from Nasdaq to the OTCBB during the same trading day.

Beginning of FAQ OTCBB

II. What is the difference between the OTC market and a stock exchange?

Stock exchanges have specific quantitative and qualitative listing and maintenance standards which are stringently monitored and enforced. Companies listed on an exchange have reporting obligations to the exchange and a direct business relationship exists between the exchange and its listed companies. The OTC market consists of unlisted securities. Issuers of these securities often have no reporting obligations to any federal regulatory authority. There are no minimum required standards and no business relationship exists between the quotation services (OTCBB, "Pink Sheets") and the issuers.

Beginning of FAQ OTCBB

III. How does the OTCBB differ from the Pink Sheets?

The OTCBB and the "Pink Sheets" are competing quotation services for OTC equity securities. The "Pink Sheets" are operated by the National Quotation Bureau, LLC (NQB) and are a static paper quotation medium printed weekly and distributed to broker/dealers while the OTCBB displays electronic real-time quotes, last-sale prices, and volume information for domestic securities, foreign securities, and ADRs.

Beginning of FAQ OTCBB

IV. What is an other-OTC security?

All OTC equity securities which are not quoted on the OTC Bulletin Board and are eligible for trade reporting on the Automated Confirmation Transaction ServiceSM (ACTSM) are categorized as other-OTC. This includes, but is not limited to, securities quoted on the Pink Sheets. Please see the FAQ regarding the **download of all other-OTC securities** from the symbol directory.

Beginning of FAQ OTCBB

V. What are the listing requirements for the OTCBB?

Because the OTCBB is a quotation service for NASD Market Makers, not an issuer listing service or securities exchange, there are no quantitative listing requirements that must be met by an OTCBB issuer. However, new Eligibility Requirements are in effect for both foreign and domestic issuers. Effective April 1, 1998, all foreign issues and ADRs must be registered with the Securities & Exchange Commission (SEC) pursuant to Section 12 of the Securities Exchange Act of 1934. Effective January 4, 1999, domestic issues quoted on the OTCBB are limited to the following securities:

- securities of issuers that make current filings pursuant to Section 13 or 15(d) of the Securities Exchange Act ("Act");
- securities of depository institutions that are not required to make filings under the Act, but file publicly available reports with their appropriate regulatory authorities;
- securities of registered closed-end investment companies; and
- securities of insurance companies that are exempt from registration under Section 12(g)(2)(G) of the Act.

OTCBB issuers do not need to send copies of the quarterly or annual filings to either the NASD, The Nasdaq Stock Market, Inc. or the OTCBB.

Beginning of FAQ OTCBB

VI. Are there trading halts on OTCBB securities?

Trading can be halted on OTCBB securities, however, neither The Nasdaq Stock Market, Inc. nor the NASD has the authority to do so. Trading in an OTC security may only be halted by the SEC.

Beginning of FAQ OTCBB

VII. What are the quotation increments/minimum quote size for OTCBB securities?

The minimum quotation size requirements for OTC equity securities vary depending on the price of the quote. Please see **Rule 6750** for further details.

Beginning of FAQ OTCBB

VIII. How do I withdraw from an OTCBB stock?

From the Nasdaq Workstation II™, click on "MarketMaking" from the top menu bar. Then, click on "Update." Type in the number "3 + the stock symbol" in the Security ID field. Tab down into the "State" field and type in a "W" then click on the "Send" button. You are now withdrawn from the stock.

Beginning of FAQ OTCBB

IX. How can I get trade and quote data for OTCBB securities?

Current and delayed trade and quote information are available for OTCBB securities from some market data vendors. Please visit our **Vendor Page** for information on contacting these data vendors.

Beginning of FAQ OTCBB

X. Where can I get historical trade and quote data for OTCBB securities?

The OTCBB Research Service offers a variety of standardized and customized research reports for OTCBB securities. Please visit our **Research Services Page** for information on the reports and research that are available from the Service.

Beginning of FAQ OTCBB

XI. How does a company get on the OTCBB?

Please visit our **How To Quote Securities Page** in Market Maker Services for detailed information on quoting a security on the OTCBB.

Beginning of FAQ OTCBB

XII. Are there filing requirements for OTCBB issuers?

No. OTCBB issuers have no filing or reporting obligations to The Nasdaq Stock Market, Inc. or the NASD, however, many OTCBB companies currently file with the SEC or other regulatory authority. Any security which begins quotation on the OTCBB after January 4, 1999, must make periodic filings with the SEC or other regulatory authority. SEC filings may be retrieved online from the **SEC EDGAR Database**.

Beginning of FAQ OTCBB

XIII. Where can I get phone and address information for an OTCBB issuer?

OTCBB issuers are not required to maintain current address and contact information with The Nasdaq Stock Market, Inc. or the NASD. This information is available, however, for many OTCBB issuers. The **1997 and 1998 Stock Summaries**, accessible from the Market Statistics area of this Web site, includes the trading symbol, name and annual summary trading statistics for every security quoted on the OTCBB as of December 31st of the year you select. Address and contact information are also included when available. This online Stock Summary replaces the annual print publication of *The OTC Bulletin Board Fact Book and Company Directory*.

Beginning of FAQ OTCBB

XIV. Can a company be delisted?

Not at this time. All OTCBB issues, however, must maintain at least one registered Market Maker in a security withdraws from the stock, the issue is removed from the OTCBB. Beginning July 1999, the OTCBB will begin to phase-out, or delist, securities of issuers who do not meet the new **Eligibility Requirements**. This phase-out will occur over a 12 month period from July 1999 through June 2000 according to the **Phase-In Schedule** published on this site.

Beginning of FAQ OTCBB

XV. What is a Form 211?

The Form 211 is the form which must be completed and submitted to the NASD Regulation, Inc. OTC Compliance Unit to initiate or resume quotations in the OTCBB, the NQB "Pink Sheets", or any other comparable quotation medium. To view or print the Form 211, please visit our **Market Maker Services Forms Page**.

Beginning of FAQ OTCBB

XVI. Why don't I receive Inside Quote information for all OTCBB securities?

At least two Market Makers must post both bid and ask quotations to calculate the inside market for a security. Because only one Market Maker is required to keep a security on the OTCBB and Market Makers are permitted to post one-sided quotes and unpriced indications of interest, there may be securities for which inside quotes can not be calculated.

Beginning of FAQ OTCBB

XVII. Who is responsible for regulating the OTCBB?

NASD Regulation regulates the quotation activity and trade practices of OTCBB Market Makers. OTCBB issuers are not regulated by The Nasdaq Stock Market,

Inc., the NASD, or NASD Regulation.

Beginning of FAQ OTCBB

XVIII. How can I get my URL included on the OTCBB.com vendor list?

The OTCBB Web site features hot links to authorized real-time and delayed vendors of market data from the **Vendor Information** section of this site. To be included on the vendor link page, you must read, complete, and sign the Corporate URL Address Authorization Form (click **here** for a PDF version of the form). Please fax the completed form, along with samples of your data display, to **Nasdaq Trading and Market Services** at (202) 728-8206. Allow two weeks for processing.

Beginning of FAQ OTCBB

XIX. Can an issuer reserve a symbol?

No, symbols may not be reserved for OTC securities. A symbol preference can be requested on the Form 211. If a requested symbol is not reserved for use on Nasdaq or restricted, we will advise the issuer that the symbol is available at that time, but that we reserve the 'right' to change their symbol should a Nasdaq applicant want to use it. There can be no guarantee that the OTC issuer will retain that symbol indefinitely.

Beginning of FAQ OTCBB

XX. How are symbols assigned?

If a requested symbol is not available, one will be assigned. Generally, the symbol assigned begins with the first letter of the first name of the issue. Reserved or restricted symbols can never be used. Any issuer may contact Market Operations at (203) 375-9609 to ask whether a symbol is available.

Beginning of FAQ OTCBB

XXI. Do I have to file a Form 211 for a New York Stock Exchange or American Stock Exchange delisted security?

Yes. Prior listing on NYSE or AMEX does not exempt a Market Maker from the Form 211 filing requirement.

Beginning of FAQ OTCBB

XXII. Do financials submitted with the Form 211 have to be audited?

Yes, the periodic reporting requirements under Sections 13 or 15(d) of the new **Eligibility Rule** require annual audits of an issuer's financial statements.

Beginning of FAQ OTCBB

XXIII. What is the source of historical OTCBB trading data?

Historical OTCBB trading data is retrieved from a database which is populated daily from files which are generated from ACT trade reports. When working with historical OTCBB trade data, it is important to note that the data is not limited to media reported activity, and that cancelled trade information is not consistently captured.

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