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Facebook and the Challenge of Staying Private

Private companies have always struggled with staying below the 500-shareholder threshold that would trigger reporting obligations. Increasingly liquid secondary markets for private company securities and regulatory uncertainty over counting shareholders have increased the challenge. Added to this is the ability under current SEC rules for third-parties to blow an otherwise carefully executed private offering by leaking details of the offering, and some private companies may wonder whether staying private is worth the trouble.

By Scott D. McKinney

A private company, such as Facebook, must constantly monitor and manage the number of holders of each class of its outstanding equity securities to reduce the chance of becoming a reporting company on a timeline not of its own choosing. Section 12(g) of the Securities Exchange Act of 1934 (Exchange Act) and the rules thereunder require that a company with more than \$10 million in assets and 500 or more shareholders of

record of a class of equity security¹ at the end of its fiscal year register the security under the Exchange Act and start filing periodic reports with the U.S. Securities and Exchange Commission (SEC). Historically, private companies would have conducted an initial public offering before that 500-shareholder threshold is at risk of being crossed. With the burden of being a reporting company, the state of the economy, founders maintaining large share ownership, the ability to raise capital privately, and still evolving business models, companies are attempting to stay private longer.

The delay in going public has put pressure both on existing shareholders who are looking for an exit strategy (e.g., employees and former employees who need to diversify and venture capitalists who are not long-term holders) and prospective investors who want to get in as early as they can on the next hot company. Two private exchange platforms—SecondMarket and SharePost—are matching purchasers who are accredited investors with sellers who are permitted to sell. Though the volume remains thin, the number of transactions is increasing each month,² generally leading to the further distribution of shares and a greater risk of companies crossing the 500-shareholder threshold.

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A number of smaller Wall Street firms have been forming funds specifically to purchase

shares of certain private companies offered on SecondMarket and SharesPost (e.g., Facebook funds and Twitter funds).³ While a fund would ordinarily count as a single holder of record for purposes of the Section 12(g) 500-shareholder test,⁴ to the extent a private company knows or has reason to know that the selection of a form of holding securities, such as a fund, was made “primarily to circumvent” the provisions of Section 12(g) of the Exchange Act, the beneficial owners of such private company securities (i.e., the fund investors) are deemed to be the record owners thereof for purposes of Section 12(g).⁵

Facebook’s recent stock sale in which Goldman Sachs completed an offering to its non-U.S. clients of a fund that invested \$1 billion in Facebook Class A common stock raises many of these and other issues relative to private companies staying private: Should the Goldman fund count as a single shareholder or must Facebook look through the fund and count its holders as individual Facebook shareholders for the 500-shareholder test? Is it feasible for a well-known private company, such as Facebook, to conduct a private offering in the U.S. without blowing the no general solicitation requirement in Regulation D?

The SEC is apparently interested in these questions. According to press reports, the SEC contacted Goldman to inquire about several issues, including the structure of the Facebook deal and media reports about the offering.⁶ Prior to the Goldman deal, the SEC had taken an interest in secondary markets for private company securities, such as Facebook. It was reported that the SEC had sent inquiries to several participants in the buying and selling of stock of Facebook, Zynga, Twitter and LinkedIn in secondary markets like SecondMarket and SharesPost.⁷ Moreover, SharesPost’s President has stated that SharesPost is in a constant dialogue with the SEC about what is happening on its exchange platform and how SharesPost is building its platform to support trading of private companies.⁸

These factors are making it more challenging for a private company to stay private. While Facebook has announced that it expects to exceed the 500-shareholder threshold in 2011 and become a public company in 2012,⁹ its experience and that of other private companies in attempting to stay under the 500-shareholder limit, is instructive.

500-Shareholder Test and Rule 12g5-1

Under Section 13(a) of the Exchange Act, every company that has a class of securities registered under Section 12 of the Exchange Act must file periodic reports. Such issuers broadly fall into two categories: (1) issuers who have registered a class of securities under Section 12(b) so that the securities can be listed on a stock exchange; and (2) issuers who have registered a class of securities under Section 12(g) because the company had total assets of more than \$10 million and a class of equity securities held by 500 or more record holders as of the last day of the company’s fiscal year. While a company has complete control over whether and when to list a class of securities on a stock exchange, it has less control over when the number of shareholders crosses 500. Consequently, a company could be required to start filing periodic reports on a timeline that is not of its own choosing.

If a company with total assets exceeding \$10 million has 500 or more record holders of a class of equity on the last day of its fiscal year, it must within 120 days of such date register such security under the Exchange Act with the SEC by filing a registration statement, typically on Form 10. Such registration statement is effective within 60 days of filing or such shorter time directed by the SEC.¹⁰ If a company is required to undertake the effort to become a reporting company, the company will often decide to conduct a public offering of securities at the same time to take advantage of public interest in the company.

Securities are deemed to be “held of record” by each person who is identified as the owner of such securities on records maintained by or on behalf of

the issuer, provided that securities identified as held of record by a corporation, a partnership, a trust whether or not the trustees are named, or other organization are considered held by one person.¹¹ Rule 12g5-1 does not require an issuer to look through record ownership of such entities to the beneficial holders in determining whether it has 500 security holders for purposes of registration under Section 12(g) of the Exchange Act.¹² However, if the issuer knows or has reason to know that the form of holding securities of record is used “primarily to circumvent” the provisions of Section 12(g) of the Exchange Act, the beneficial owners of such securities are deemed to be the record owners thereof.¹³

Certain smaller Wall Street firms, including GreenCrest Capital, Felix Investments, and EB Exchange Funds, are creating investment funds to acquire blocks of stock of private companies.¹⁴ A special purpose LLC would own the shares of the private company stock, and investors would buy shares in the LLC. The pooled vehicles being set up to acquire a private company’s stock could push the company’s shareholder count above 499 if the SEC counted the number of investors in the funds. However, companies setting up the LLCs have stated that since the private companies are not involved in setting up the LLCs, the SEC would have a difficult time proving that the LLCs are trying to circumvent the shareholder count trigger.¹⁵

It has been reported that the SEC’s inquiry regarding Goldman’s involvement in the Facebook offering has focused in part on whether funds are being used to purchase shares “primarily to circumvent” the provisions of section 12(g) of the Exchange Act. “Primarily to circumvent” is a facts and circumstances test. Other purposes of investing through a special purchase investment vehicle could include: (1) serving as the mechanism for locking up holders; (2) delegating management of the interest in Facebook to a fund manager (as a sort of proxy voting arrangement); and (3) generating fees for the fund manager. Goldman Sachs is charging 0.5 percent of any capital committed to the investment vehicle as an “expense reserve”

as well as a 4 percent placement fee and 5 percent of any gains.¹⁶ Facebook benefits by only having to deal with one new shareholder, the Goldman fund. Certainly, with regard to private offerings of new shares, the SEC does not want to interfere with legitimate capital raising activities of private companies. It has been noted that the whole venture capital industry is based upon funds investing in private companies.¹⁷

Given the uncertainty associated with the possibility of the SEC second-guessing whether the selection of a form of holding securities was made “primarily to circumvent” the provisions of Section 12(g) of the Exchange Act, the determination of the number of holders that should count for purposes of Section 12(g) is a topic ripe for the SEC to weigh-in with an interpretive release or clarification through rule-making.

Strategies to Stay Under 500 Shareholders

Facebook and other private companies actively manage their activities so as to stay under the 500-shareholder threshold. While it is possible to reduce the possibility of inadvertently crossing the 500-shareholder threshold, many private companies do not realize they should be concerned with this until they have been raising capital and issuing equity awards to employees for some time. In any event, startup venture capitalists will generally not agree to be forgo selling their shares “unless and until the private company becomes a reporting company.” Also, most startup private companies, many with unproven business models, are more concerned with making payroll than possibly having to become a reporting company earlier than they would otherwise prefer. Nevertheless, there are methods that Facebook and other private companies use to stay under the 500-shareholder threshold.

Private Investment by Funds

While selection of a form of holding securities, such as a fund, may not be made “primarily

to circumvent” the provisions of Section 12(g) of the Exchange Act, there is an advantage to a fund counting as a single holder of record for a company trying to stay private. This certainly can be one of the criteria evaluated in determining how to structure a private offering or, to the extent the issuer is involved, a secondary market purchase. Where there are other reasons to make the investment through a fund, companies, and investors should not feel intimidated from using a fund structure. Caution should be exercised, however, in circumstances where an investment through a fund is not a customary investment structure or there is no other business reason for using such a structure.

Stock Options

When private companies grant stock options, they must consider compliance with both the Securities Act of 1933 (Securities Act) and the Exchange Act. Rule 701 under the Securities Act provides an exemption from the registration requirements of the Securities Act for stock option grants that comply with such rule. For purposes of the 500-holder test under the Exchange Act, stock options, including compensatory employee stock options, are considered a separate class of equity security. Since late 2007, the SEC has had an exemption from the registration requirements of Section 12(g) of the Exchange Act for compensatory employee stock options issued by non-reporting companies.¹⁸ Specifically, under the Rule 12h-1(f) exemption: (1) compensatory stock options must be issued under a written plan; (2) plan participants must be limited to employees, directors, and other service providers of the issuer, its parents or its subsidiaries; (3) the securities underlying all of an issuer’s compensatory stock options be of the same class of securities; (4) there must be certain transfer restrictions;¹⁹ and (5) the company must agree in the plan or an agreement to provide, every six months, the risk and financial information required under SEC Rule 701 if securities sold in reliance on that rule in a 12-month period exceeded \$5 million.

The exemption does not extend to the class of securities underlying the issuer’s compensatory employee stock options.

Right of First Refusal and Share Repurchases

Many companies, including Facebook, have the right of first refusal to buy any shares of their stock offered on the private exchanges or otherwise.²⁰ Facebook has the option to either buy the stock itself or find another buyer within 30 days who is willing to pay the same price.²¹ Certain private companies also occasionally offer to repurchase securities that have been issued to employees. However, share repurchases are maybe not the best use of a late-stage startup/early growth company’s funds.

Restricted Stock Units

In 2007, Facebook stopped issuing stock options or shares to new employees, instead giving them restricted stock units that do not have value unless the company goes public or is sold.²² A restricted stock unit is essentially a promise to delivery shares of stock in the future, subject to the satisfaction of any vesting requirements. Because restricted stock units are considered an equity security for purposes of Section 12(g) and the existence of 500 or more record holders of such securities at the end of Facebook’s fiscal year would itself trigger the obligation to become a reporting company, Facebook sought and obtained SEC Staff no-action relief from the Exchange Act registration requirements of Section 12(g) with respect to the restricted stock units.²³

Insider Trading Policy; Locking Up Employees

In March 2010, Facebook announced a ban on current employees selling stock.²⁴ In April 2010, Facebook put in place an insider trading policy that prohibits current employees from selling shares unless the company opens a trading window. (In addition to slowing the distribution

of Facebook securities, the insider trading policy is helpful in preventing employees from trading on material non-public information.) This insider trading policy effectively eliminates the possibility of current employees selling shares, as Facebook has not opened a trading window, which caps the amount of stock available in the secondary market to those shares held (or formerly held) by former employees.

Assisting Employees with Resale of Stock

In 2009, Facebook arranged a program for employees to sell at least \$100 million in shares to Russian investment firm Digital Sky Technologies, which also invested \$200 million directly in Facebook.²⁵ With this program, Facebook was able to relieve some of the pressure of holders who wanted to sell shares while avoiding a broad distribution of those shares. In fact, this arrangement likely reduced the number of existing shareholders.

Exorbitant Share Transfer Fees

While the issuance of restricted stock units and the new insider trading policy may have effectively curbed sales by current Facebook employees, former employees are still able to sell their shares in the secondary markets. To discourage such sales by employees, Facebook and Zynga are charging exorbitant transfer fees for each sale of company shares. Zynga began imposing a fee of \$4,500 for each private share transaction in August 2010, and raised it to \$6,000 per sale in September.²⁶ Facebook began imposing a \$2,500 fee in October 2010.²⁷ A Zynga representative indicated that Zynga charges a fee for the transfer of stock to cover some of the costs associated with arranging and overseeing sales of company stock.²⁸

Optional or Redemption by the Company

A strategy that has been adopted by Roche Capital Corporation is to include a provision in its certificate of incorporation that provides that

if the 500-shareholder threshold is crossed for a specified class of equity, than the issuer has the option to redeem such shares in a manner that results in fewer than 500 record holders of the class remaining.²⁹

Reverse Stock Split

More often used in connection with going private, another manner of reducing the number of shareholders is a reverse stock split, which requires an amendment to the issuer's certificate of incorporation. As an example, in a 1:1,000 reverse stock split, persons with less than 1,000 shares would be cashed out. However, like share repurchases generally, the required payments for resulting fractional shares may not be the best use of company funds. Also, such a reverse stock split would likely not endear the company to its employees holding less than 1,000 shares. That being said, the tactic of effecting a reverse stock split to avoid becoming a reporting company has been used to counter a shareholder who has distributed small amounts of shares to numerous persons in attempt to cause an issuer to become a reporting company.

Secondary Market Exchange Platforms

Complicating the efforts of Facebook and other private companies to stay private is the increased liquidity in secondary markets for private company securities that has resulted from the growth of private exchange platforms, such as SecondMarket and SharesPost. NYPPEX, a secondary market maker, reports that 2010 secondary market transaction volume was up 79 percent year-over-year to total \$22.1 billion. In 2010, SecondMarket executed over \$400 million in trades involving about 40 private companies, compared to executing about \$100 million in trades in 2009.

The Securities Act registration exemptions that buyers and sellers use for sales on SharesPost and SecondMarket are the Section 4(1) exemption,³⁰

and in some cases, Rule 144.³¹ Buyers are typically persons qualified as accredited investors. It could be said that these exchange platforms are generally doing for resales of private company securities to accredited investors what exchange platforms like PORTAL Alliance³² do for resales of 144A³³ securities to qualified institutional buyers and qualified purchasers.³⁴ However, unlike in 144A resales,³⁵ in the case of resales on SharesPost or SecondMarket there is often little information available concerning the issuer, other than third-party research reports containing best guesses on revenues, earnings, and capitalization.

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Recently, SecondMarket and SharesPost have been offering auctions of private-company stock to simplify the matching process.³⁶ SharesPost has structured auctions as follows: The auction is held for a week and begins with SharesPost putting a call out to sellers to participate.³⁷ Within a couple days, SharesPost then informs buyers of the number of shares available and the reserve price.³⁸ That leaves buyers with 2 to 3 days to bid on the shares. The auction is conducted “on a sealed bid basis” and is only open to accredited investors. If the reserve price is met by persons willing to purchase a threshold number of shares, winning bidders are sold interests in an LLC that invests in the private company.

Facebook’s Recent Private Offering

On January 21, 2011, Facebook announced that it had received \$1 billion from Goldman Sachs in a Regulation S offering, on the heels of an SEC inquiry.³⁹ Goldman Sachs sold interests to its non-U.S. clients in a fund (a special purpose

vehicle) that invested \$1 billion in Facebook Class A common stock.⁴⁰

The SEC had opened an inquiry into the structure of the offering and whether it violated the law because of widespread news coverage.⁴¹ With regard to the widespread news coverage, the SEC was no doubt concerned that the hype would result in a “conditioning of the market” for the offering, regardless of the precautions taken by Facebook and Goldman. In addition, with regard to the structure of the offering, the SEC was again asking questions about whether the use of a fund as the investment vehicle was intended “primarily to circumvent” the provisions of Section 12(g) or 15(d) of the Exchange Act.

Goldman originally had opened the offering to both its U.S. clients and its non-U.S. clients. According to reports, the offering to U.S. clients was to be conducted pursuant to Rule 506 of Regulation D, a safe harbor available to issuers for the private offering exemption of Section 4(2) of the Securities Act. Section 4(2) exempts from the Securities Act’s registration requirements “transactions by an issuer not involving any public offering.” Section 4(2) does not provide specific guidelines regarding how a private placement avoids involving a public offering. “Safe harbor” means that a private securities offering that follows the requirements set forth in Reg. D Rule 506 is automatically in compliance with the requirements of Section 4(2). Companies using the Rule 506 exemption can raise an unlimited amount of money.

Rule 502 under Regulation D prohibits the use of a “general solicitation or general advertising” in a Rule 506 offering of securities. “General solicitation” is generally the use of mass media, seminars or other similar marketing techniques to sell the securities or to condition the market for their sale. Conditioning the market refers to anything that, “even though not couched in terms of an express offer, conditions the public mind or arouses public interest in the particular

securities.”⁴² The SEC believes that whether a particular action is a general solicitation is generally an issue of facts and circumstances.

While an offering of securities to the general public would be a prohibited general solicitation, an issuer may offer securities to those with whom the issuer has a pre-existing and substantial relationship. To be pre-existing, at a minimum the relationship must have been established at least 30 days prior to the offering. To be substantial, an issuer’s relationship must be such that the issuer is fully aware of the financial circumstances or sophistication of the potential investor. Since many issuers do not have pre-existing relationships with large numbers of investors, they often hire a broker-dealer that has such relationships, such as Goldman.

The SEC was no doubt concerned that the hype would result in a “conditioning of the market” for the offering.

While the SEC has offered some guidance on what constitutes general solicitation or advertisement, the question of whether the issuer or anyone on its behalf tries to create ‘hype’ or interest in the offering is very fact specific. There may be a general solicitation if too many parties are invited to consider making the investment or the existence of a pending private offering becomes widely known resulting in a media frenzy. In the case of Facebook’s offering, Goldman took careful steps to maintain the confidentiality of the offering and its terms. For example, it has been reported that Goldman sent copies of the private-placement memo often by messenger instead of email to reduce the chance of leaks. In some cases, even spouses of the document’s recipients were asked to sign a confidentiality agreement.⁴³ Nonetheless, someone had leaked the existence of the offering and a media circus

followed. The media hype of the offering left Facebook and Goldman Sachs with little choice but to limit the offering to non-U.S. persons outside the U.S. in compliance with Regulation S, which does not prohibit general solicitation.⁴⁴ The penalty for a blown private offering (*i.e.*, an offering that has not been registered under the Securities Act that fails to qualify for any exemption) would be that the purchasers are entitled (but not required) to rescind the transaction and obtain a refund of their purchase price or receive damages.

That Facebook and Goldman had to abandon a private offering in the U.S. due to the actions of others, resulting in an offering under Regulation S that excludes U.S. persons, is probably not the result the SEC had in mind when it adopted Regulation D. While there have been calls to reform or eliminate the “general solicitation” prohibition of Regulation D for quite some time,⁴⁵ perhaps it is time for the SEC to take a hard look at making changes to the general solicitation prohibition. Otherwise, private companies, particularly companies with a media following and the public’s interest, may be excluded from accessing U.S. private capital markets, turning to foreign investors at the exclusion of U.S. investors and possibly forcing such companies to go public on a timeline that is not of their choosing.

Conclusion

There are a number of reasons a private company would want to monitor and manage the number of holders of each class of its outstanding equity, so as to avoid having to become a reporting company on a timeline not of its own choosing. Most companies take advantage of the requirement to become a reporting company by raising capital in the public market in connection with becoming a reporting company. In this regard, it is generally helpful to have maybe a couple years of profits, or finances moving in the direction of profits, prior to going to the public capital market. Fortunately, there are a number

of strategies private companies can follow, of varying degrees of aggressiveness, to stay below the 500-shareholder threshold.

The question of whether the issuer or anyone on its behalf tries to create ‘hype’ or interest in the offering is very fact specific.

The evolving secondary markets for private company securities are making management of the shareholder count much more complex. Also, unless the SEC provides guidance or clarification through rulemaking, there will continue to be uncertainty whether the selection of a form of holding securities, such as a fund, will be deemed by the SEC to have been made “primarily to circumvent” the provisions of Section 12(g) of the Exchange Act, such that the 500-shareholder threshold might be inadvertently crossed. Moreover, with the increasing interconnectedness of society (through, for instance, smart phones, blogs, and the 24-hour news cycle) and the desensitization of society to issues of privacy and confidentiality (through the growing popularity of social media), the existing “general solicitation” prohibition is becoming more and more an impediment to private capital formation in the U.S. This leaves companies with no alternative but to turn to foreign markets or, possibly at a less than opportune time, the U.S. public market. As Facebook has discovered, staying public can be quite a challenge.

NOTES

1. Section 3(a)(11) of the Exchange Act defines “equity security” as “any stock or similar security... or any security convertible, with or without consideration, into such a security.”
2. Per Lattman, “Stock Trading in Private Companies Draws S.E.C. Scrutiny,” *The New York Times’ DealBook* (December 27, 2010) (Trading Draws S.E.C. Scrutiny Article).
3. *Id.*
4. Rule 12g5-1(a)(2) under the Exchange Act (Rule 12g5-1(a)(2)).
5. Rule 12g5-1(b)(3) under the Exchange Act (Rule 12g5-1(b)(3)).
6. Sam Gustin, “Goldman-Facebook Deal Draws SEC Scrutiny of Startup Investing,” *Wired.com* (January 5, 2011).
7. Trading Draws S.E.C. Scrutiny Article.
8. Gennie Kelly, “Private Exchange’ in Dialogue with SEC: President Share, Post” *CNBC* (December 29, 2010).
9. Facebook press release dated January 21, 2011.
10. Section 12(g)(1) of the Exchange Act.
11. Rule 12g5-1(a)(2).
12. SEC Compliance and Disclosure Interpretation No. 252.01 (September 30, 2008).
13. Rule 12g5-1(b)(3).
14. Trading Draws S.E.C. Scrutiny Article.
15. Kerry A. Dolan, “Frenzy for Facebook Shares Heats Up With a New Auction,” *Forbes* (December 13, 2010).
16. Max Abelson and Chritine Harber, “Goldman Sachs May Sell or Hedge Facebook Stake Without Warning,” *Bloomberg* (January 6, 2011).
17. Joshua Gallu and Jesse Hamilton, “Facebook May Face SEC Disclosure Scrutiny as Goldman Invests \$450 Million,” *Bloomberg* (January 3, 2011).
18. Prior to adoption of Rule 12h-1(f) under the Exchange Act, the SEC’s Division of Corporation Finance provided no-action letter relief to private, nonreporting companies faced with registration under Section 12(g) of the Exchange Act solely due to their compensatory employee stock options being held by 500 or more holders of record (and having more than \$10 million in assets), subject to meeting certain criteria, based on the reasoning that the characteristics of many employee benefit plans—which are by their own terms limited to employees, not available to the general public, and subject to transfer restrictions—obviate the need for applicability of all the rules and regulations aimed at public trading markets.
19. Pursuant to Rule 12h-1(f) under the Exchange Act, the option grantee must be prohibited from transferring the option other than: (1) to certain family members through gifts or pursuant to domestic relations orders; (2) to an executor or guardian upon the grantee’s death or disability; (3) to the issuer (including but not limited to transfers upon the issuer’s contractual right to repurchase the securities); or (4) in connection with a change of control or other acquisition of the issuer if, after such transaction, the issuer will no longer be relying on this exemption. The transfer restriction applies both to the option and (until the option is exercised) shares issuable upon exercise of the option.
20. Trading Draws S.E.C. Scrutiny Article.
21. Pui-Wing Tam and Geoffrey A. Fowler, “Hot Trade in Private Shares of Facebook,” *The Wall Street Journal* (December 28, 2010) (Hot Trade Article).
22. Trading Draws S.E.C. Scrutiny Article.

23. See Facebook, Inc., SEC Staff No-Action Letter (October 14, 2008). Section 12(h) of the Exchange Act allows the Staff to exempt an issuer from the registration requirements of Section 12(g) if it finds, “by reason of the number of public investors, amount of trading interest in the securities, the nature and extent of the activities of the issuer, income or assets of the issuer or otherwise, that such action is not inconsistent with the public interest or the protection of investors.”
24. Trading Draws S.E.C. Scrutiny Article.
25. Hot Trade Article.
26. Douglas MacMillan, “Facebook, Zynga Impose Fees on Private Sales of Shares,” Bloomberg Businessweek (October 11, 2010).
27. *Id.*
28. *Id.*
29. See Certificate of Designation of Limited Conversion Preferred Stock of Roche Capital Corporation filed as Exhibit 4 to the Company’s F-4 registration statement filed with the SEC October 6, 1994.
30. Under Section 4(1) of the Securities Act, an investor may resell securities in a non-public exempt transaction if that investor is not an “issuer, underwriter or dealer,” as those terms are defined by the Securities Act. Under Section 2(a)(11) of the Securities Act, any purchaser that purchases securities from an issuer “with a view to,” or offers or sells securities for the issuer in connection with, a “distribution” of the securities is an “underwriter” without the benefit of any other exemption under Section 4 of the Securities Act.
31. Rule 144 under the Securities Act provides a nonexclusive safe harbor from being an “underwriter” for holders of “restricted securities” (securities acquired directly from the issuer in a transaction exempt from registration) and “control securities” (securities held by affiliates of the issuer acquired in secondary market transactions). The safe harbor enables selling security holders to use Section 4(1) of the Securities Act for the resale by complying with Rule 144. For non-affiliates of a non-reporting company, Rule 144 requires that the security be held for at least one year.
32. The PORTAL Alliance Platform is owned by The PORTAL Alliance LLC, whose founding members consist of BofA Merrill Lynch, Citi, Credit Suisse, Deutsche Bank, Goldman Sachs, J.P. Morgan, Morgan Stanley, The NASDAQ OMX Group, Inc., UBS, and Wells Fargo Securities.
33. Rule 144A under the Securities Act allows for the immediate resale of private placement securities among qualified institutional buyers (generally institutions that manage at least \$100M in securities) without requiring SEC registration. See Rule 144A(a)(1) under the Securities Act.
34. Section 3(c)(7) of the Investment Company Act of 1940.
35. To satisfy Rule 144A, if the issuer is not a reporting company under the Exchange Act, the holder of the securities and any prospective purchaser designated by the holder must have the right to obtain from the issuer, upon request of the holder, the following information: (1) a brief description of the issuer’s business, products, and services; (2) the issuer’s most recent balance sheet, profit and loss statement, and retained earnings statement (the financial statements must be audited if audited statements are “reasonably available”); and (3) similar financial statements for the two preceding fiscal years. See Rule 144A(d)(4)(i) under the Securities Act. The information must be “reasonably current” in relation to the date of resale under Rule 144A. See Rule 144A(d)(4)(ii) under the Securities Act.
36. Hot Trade Article.
37. Dawn Kawamoto, “Facebook Shares Clear \$25 in SharesPost Auction,” DailyFinance.com (December 17, 2010).
38. *Id.*
39. Facebook press release dated January 21, 2011.
40. *Id.*
41. Andrew Ross Sorkin, “Goldman Limits Facebook Investment to Foreign Clients,” The New York Times’ Dealbook (January 17, 2011) (Investment Limited to Foreign Clients Article).
42. S.E.C. Release No. 33-3844 (October 8, 1957).
43. Anupreet Das, Geoffrey A. Fowler, and Liz Rappaport, “Facebook Sets Stage for IPO Next Year,” The Wall Street Journal (January 6, 2011).
44. Investment Limited to Foreign Clients Article.
45. See, e.g., William K. Sjostrom, “Relaxing the Ban: It’s Time to Allow General Solicitation and Advertising in Exempt Offerings,” Florida State University Law Review, Vol. 32, No. 1, 2004. Available at SSRN: <http://ssrn.com/abstract=834244>; and Patrick Daugherty, “Rethinking the Ban on General Solicitation,” 38 Emory L.J. 67, 115-123 (1989).

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