Wednesday, October 3, 2012
9:00 AM - 10:30 AM

408 – Taking Your Company Public

Delida Costin
General Counsel
Pandora Media, Inc.

Jeff Hoffmeister
Managing Director
Morgan Stanley, Investment Banking Division

Lior Nuchi
Partner
Alston & Bird LLP

James Williams
Vice President, General Counsel & Corporate Secretary
Liquidity Services, Inc.

Michael Wu
General Counsel
Rosetta Stone

Faculty Biographies

Delida Costin

Delida Costin is the general counsel of Pandora where she manages the company's legal department. Before Pandora, Ms. Costin maintained a private legal practice and served as a member of the attorney bench at Axiom Legal. Prior to that, she was vice president and assistant general counsel at CNET Networks. During the years of her practice, she has advised on issues related to compliance, securities, digital media, privacy and data protection, and online advertising.

Ms. Costin received her bachelor's degree from Northwestern University and her JD from Boston University School of Law. She has practiced with the law firms of Goodwin, Procter LLP in Boston, and Pillsbury Winthrop Shaw Pittman LLP in Palo Alto, CA.

Jeff Hoffmeister

Jeff Hoffmeister is a managing director in Morgan Stanley's New York office where he leads Morgan Stanley's east coast technology banking team.

Mr. Hoffmeister also served as head of Morgan Stanley's European tech banking franchise. Prior to joining Morgan Stanley, he worked at Raymond James Financial, Anheuser-Busch Inc.'s M&A department, and in the auditing and consulting divisions of PricewaterhouseCoopers LLP.

Mr. Hoffmeister is an active volunteer with the Salvation Army, and has done extensive work with the organization.

Mr. Hoffmeister received a BSBA in finance from Georgetown University.

Lior Nuchi

Lior O. Nuchi is a partner at Alston & Bird. Mr. Nuchi has practiced corporate law in Silicon Valley for close to 25 years. He focuses on complex transactions for a variety of clients, including corporations, investment firms, investment and commercial banks, universities and individuals. Mr. Nuchi has represented many companies in corporate and finance matters ranging from mergers and acquisitions to seed-round financings and initial public offerings. He regularly advises CEOs, boards of directors and special committees on strategic and corporate governance issues and securities law matters, and he has represented clients in more than 100 public and private company acquisitions, strategic alliances and financings, ranging in size from several billion dollars to start-up transactions.

Mr. Nuchi has worked on over 30 IPOs for a wide range of companies in the technology, life sciences, media, entertainment and retail markets based throughout the U.S. and Canada, Mexico, Brazil, Europe, Israel, China, Japan and India.

Since the early 1990's, Mr. Nuchi has participated in many of the most important transactions that have created the commercial Internet and currently is engaged in cutting-edge transactions bringing video and other broadband services to the Internet, as well as working in the wireless industry.

Mr. Nuchi received his JD from the New York School of Law and his BA from Columbia University. He is fluent in German, Hebrew and Japanese.

James Williams

James E. Williams is the vice president, general counsel and corporate secretary of Liquidity Services, Inc., a Nasdaq listed company headquartered in Washington, D.C. Liquidity Services provides business and government clients and buying customers the world's most transparent, innovative and effective online marketplaces and integrated services for surplus assets. Mr. Williams is responsible for all legal, corporate governance and compliance matters at Liquidity Services.

Prior to joining Liquidity Services, Mr. Williams served as vice president, general counsel and secretary of Acterna Corporation, a telecommunications equipment manufacturer. Prior to Acterna, he served as assistant general counsel of Pathnet Telecommunications, a wholesale telecommunications provider. Mr. Williams began his career in private practice; he was a corporate associate with the law firms of Kirkland & Ellis and Wilson Sonsini, Goodrich & Rosati.

Mr. Williams is a member of ACC's WMACCA Chapter and is a member of its board of directors.

He received his BA from Brown University and his JD from the University of Chicago Law School.

Michael Wu

Michael Wu is responsible for all legal, corporate governance, government affairs and compliance matters at Rosetta Stone Inc. When he joined Rosetta Stone, he established Rosetta Stone’s corporate compliance and corporate governance functions as well as its anti-piracy and anti-fraud enforcement program. In 2009, Mr. Wu oversaw the company’s successful initial public offering on the New York Stock Exchange.

Before joining Rosetta Stone, Mr. Wu was general counsel at Montreal-based Teleglobe International Holdings Ltd. In 2004, Mr. Wu led Teleglobe's acquisition of voice over IP provider, ITXC Corp., and the listing of the combined company on NASDAQ.

Prior to Teleglobe, Mr. Wu was a senior attorney in the Hong Kong and Reston, VA offices of Global One, the international joint venture between Sprint, Deutsche Telekom and France Telecom. He was also associated with a predecessor firm of Bingham McCutchen LLP in Washington, D.C. and Baker Botts LLP in Houston, TX, focusing on corporate transactions.

Mr. Wu is fluent in English and Mandarin Chinese. He is a member of the Association of Corporate Counsel and Northern Virginia Technology Council General Counsel Committee. He serves on the boards of the Business Software Alliance and the ACC's Washington Metropolitan Chapter.

Mr. Wu holds a JD from the University of Virginia School of Law and a BA in political science from Emory University.

Taking Your Company Public

IPO Preparation – What Must Happen Before the Kick-Off Meeting

Is Your Management Team Ready for an IPO?

- Key considerations
- Educate the management team on how the role of the chief legal officer will change

Is Your Board Ready for an IPO?

- Independence Requirements
- Need majority of the Board to be independent (phase in rules for IPO allow one year to meet requirement)
- Most common bars to independence:
  - being employed by the company within three years
  - providing more than $120,000 a year in consulting services to the company
  - working for a company that has transactions with the company (there are materiality thresholds)
  - having family members who are employed with the company or who do business with the company
- No director qualifies as "independent" unless the Board affirmatively determines that the director has no material relationship with the listed company (either directly or as a partner, shareholder or officer of an organization that has a relationship with the company). Companies must disclose these determinations.
- Stock ownership is typically not a bar to being considered an independent director EXCEPT that Stock ownership over 10% will typically bar independence on the audit committee.
- Committees need to be 100% independent (audit, compensation and corporate governance and nominating committees), but there are phase in rules: one independent member upon IPO, majority independent within 90 days and 100% independent within one year of listing.

Is Your Board Ready For an IPO?

- If they do not have public company experience, seek out ways to educate them
- Often, outside counsel will have a meeting with the Board to lay out their fiduciary duties
- Audit committee needs to have someone qualified as a “financial expert” and there are detailed rules as to what that entails

Getting Your House in Order

- Internal due diligence
- Regulatory compliance
- Stock records
- Related party transactions to be disclosed
- Internal controls, financials and reporting processes
  - SOX 404 certifications do not kick in until after a phase in period (second 10-K), but still have to disclose internal control problems disclosed by auditors in management letters
- Upgrading your legal staff
- Hiring IR professional

Website

- SEC staff will review your website
- Archive press releases into a separate space marked "archive" or something similar
- Scrub anything inconsistent with the registration statement
- Typically, you want to remove links to websites of unaffiliated third parties

Post-IPO Website Disclosure

- Typically, create new section called "investor relations" or something similar
- Forms 3, 4 and 5 must be posted to website
- Code of ethics and corporate governance guidelines must be posted.
- Nominating committee charter, audit committee charter and compensation committee charter must be posted
- Provide access to all '34 Act reports through link to SEC website or otherwise (there are phase in rules on compliance)
- Non-GAAP financial measures reconciliation are typically posted.
- Regulation FD disclosure items are typically posted (but posting is not necessarily sufficient by itself)

Determining Who Will Be Named Executive Officers

- Rule 402(a)(3) Disclosure shall be provided for each of the following (the "named executive officers"):
  - All individuals serving as the registrant's principal executive officer or acting in a similar capacity during the last completed fiscal year ("PEO"), regardless of compensation level;
  - All individuals serving as the registrant's principal financial officer or acting in a similar capacity during the last completed fiscal year ("PFO"), regardless of compensation level;
  - The registrant's three most highly compensated executive officers other than the PEO and PFO who were serving as executive officers at the end of the last completed fiscal year; and
  - Up to two additional individuals for whom disclosure would have been provided pursuant to paragraph (a)(3)(iii) of this Item but for the fact that the individual was not serving as an executive officer of the registrant at the end of the last completed fiscal year.
- Determination is compensation for last completed fiscal year
- Internal political considerations

Determining Who Will Be Named Executive Officers

- Need to make sure each named executive officer understands that his or her compensation will be public
- Make sure the named executive officers are aware that investment bankers will run background searches (so they should disclose any past criminal issues, bankruptcies, etc., now rather than later)

Brief Management Team About Running a Public Company

- If your management team has never run a public company before, you should brief the management team about the ongoing obligations of a public company and the enhanced scrutiny that your company will be under.
  - Periodic reporting requirements under the Exchange Act (annual report on Form 10-K, quarterly reports on Form 10-Q, material events between periodic reports on Form 8-K, etc.
  - Regulation FD compliance (disclosure of material, nonpublic information to certain "specified persons" must be made simultaneously to public)
  - Misuse of Inside Information and establishment of blackout periods several days/weeks before the end of each quarter and ending when the company's earnings is released and absorbed over one to three trading days into the public markets

Stock Option Grants

- The SEC has enhanced scrutiny of pre-IPO grants in the last few years
- In the past, companies sent separate letters to the SEC containing their cheap stock analysis
- Today, pre-IPO option awards are set forth in the body of the registration statements along with the grant date exercise price and grant date fair market value **and** you have to disclose the manner in which the valuation was done. See SFAS 123R.
- Valuations should done before grants are made
- Once you are public, consider setting regularly scheduled meetings to do grants so there is no appearance of trying to game the stock price or backdate options

Executive Compensation

- Prepare in advance for the fact that the compensation of your named executive officers will be public.
- You will have to disclose in the registration statement all bonus targets from the prior year, whether or not those targets were met, and whether and why a bonus was paid.
- The SEC is allowing very few exceptions to disclosing the performance objectives/milestones based on the information being competitively sensitive, so plan for this.
- Setting stretch goals can make it appear that the management team isn't meeting expectations. Essentially, management reviews become public.
- You must disclose how you set compensation. Do you use peer groups or benchmarking?

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Post-IPO Executive Compensation

- You will want to establish post-IPO compensation. This will need to be described in the registration statement, so you don't want to wait too long to get this in place.
- You also want to establish post-IPO Board compensation
- Consider and put in place post-IPO equity plans, employee stock purchase plans or other compensation plans
- Consider post-IPO change of control and severance agreements with executive team
- Consider post-IPO indemnification agreements with directors and officers

Positioning a Company

- Management team makes the initial determination on how to position the company in the market when meeting with investment bankers
- Positioning is subject to change after commencement of IPO process

Picking Your External Team

- Investment bankers
- Auditors
- Outside counsel
- NYSE/NASDAQ
- Transfer agent
- Financial printer

Investment Bankers

- Trend is to have more bankers on cover
- 7% fees is almost always the norm unless you have a huge deal or other special circumstances
- Considerations: reputation and expertise in the company's industry, marketing and distribution strengths, post-public offering support (research analysts, market making capabilities, strengths in other strategic areas such as M&A), level of commitment to the deal, positioning, etc.

Auditors

- You may need to transition pre-IPO team to someone with IPO experience
- Changing auditors can be very expensive and it can be time consuming to bring new team up to speed
- You don't want to have to restate financials for changes in accounting methods so it is helpful to get quality auditors on board early

Outside Counsel

- IPO experience
- Pricing flexibility
- Want someone who fits how you operate and understands your needs
- You will likely have lots of questions at all hours of the day and night – make sure your outside counsel is willing to be available and has your back

NYSE/NASDAQ

- Governance rules are now substantially the same
- Consider how much marketing/advertising and support they are willing to offer
- Consider difference in listing fees
- Consider visit to both exchanges

Transfer Agent

- Pricing, experience, customer support
- Annual meeting support
- Check references

Financial Printer

- Donnelley and Merrill are big two
- Prices highly negotiable
- Price quotes always underestimate the number of "changed pages" because of the way they count changed pages
- Obtain concessions such as waiver of periodic filing fees during first year
- Seek cap

IPO Process from Kick-Off Meeting Forward

Organizational Kick-Off Meeting

- Presentations by each functional group leader of the company: CEO, CFO, General Counsel, COO, Product Manager, Marketing Manager, etc.
- All of the bankers' team members will attend, as well as auditors, outside counsel and underwriters' counsel
- Establish the company's positioning, industry overview, competitive strengths, product roadmap, growth plans, etc.

Organizational Kick-Off Meeting

- Preferable to have distributed a preliminary draft of the registration statement or at least the business section before the meeting
- Plan to have a first drafting session on the business section at the end of the meeting, as it is a good chance to get everyone's input
- Probably the last drafting session where bankers other than the top two will participate. Opinions and deals vary on this issue.

Industry Overview

- Need a short description of the industry
- Typically want to quote third party sources for size of market, growth rates, industry drivers, so you want to start early to identify sources
- Check filings of competitors
- Bankers can help with this
- You may have to get consents to quote third party data, so it is best to identify sources and start process early

Supporting Claims

- One big responsibility of inside and outside company counsel is to make sure all statements in the registration statement are supported
- Typically, build a binder of support that can be provided to underwriters' counsel
- Any numbers that don't come from financials have to be supported somehow

Risk Factors

- Company counsel and general counsel have primary responsibility for risk factor section
- Want to think of and identify all material specific risks applicable to the company
- SEC wants you to avoid generic risks applicable to all companies
- Competitor filings can be helpful, but you have to tailor to your company – ask management what keeps them up at night
- Consider what are the current hot topics in your industry or the economy and make sure you have considered if it will have a disproportionate impact on your company (e.g. SARS a few years ago, global warming, recession)

Timeline

- From organizational meeting to filing first registration statement is typically 4 to 8 weeks, assuming you are prepared and have a first draft of registration statement ready by the organizational meeting
- First SEC Comments are due in 30 days
- Typically 4 to 6 weeks to clear all SEC comments, print reds and start road show. Typically, you will have to update financials during this time, so factor that into timetable.
- Road shows typically last a week or two. At the end, you price, start trading and print final prospectus.

Due Diligence

- Typically, you will want to set up an electronic data room so it is easy for underwriters and their counsel to access and review information. This also makes it easy for everyone to capture everything in the event of later disputes.
- Sections 11 and 12(a)(2) of the Securities Act of 1933 subject underwriters to potential liability for any material misrepresentations or omissions contained in a registration statement or prospectus. These sections also provide the underwriters with a "due diligence" defense.
- This is why underwriters and their counsel will spend so much time probing for any possible problems.
- Underwriters and their counsel will at times blow seemingly small issues way out of proportion in order to establish their defense.
- The company has no similar defense.
- The underwriters will conduct thorough background checks of directors and executive officers, so make sure your management team is aware of this up front and any issues are dealt with.

D&O Insurance

- Start early to get quotes on public company D&O insurance and have an experienced insurance lawyer review the policy for coverage and other issues

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Material Contracts

- Item 601 of Regulation S-K spells out what exhibits have to be filed with the registration statement.
- Ordinary course contracts are excluded, however, you must file contracts upon which your business is substantially dependent, as in the case of continuing contracts to sell the major part of your products or services or to purchase the major part of your requirements of goods, services or raw materials or any franchise or license or other agreement to use a patent, formula, trade secret, process or trade name upon which your business depends to a material extent.
- You can request that some specific portions of such contracts, such as trade secrets, be kept confidential by filing a request for confidential treatment with the SEC. Any such requests should accompany your first registration statement filing. This request will run in parallel with the registration statement review process.

Publicity Issues

- Once you begin to contemplate an IPO, the general counsel should make sure that all press releases and public comments are run through his office to avoid "gun jumping" concerns
- The SEC will typically review all pre-IPO publicity concerning a company and may delay an IPO to "cool off" the market if it believes that the company has been improperly "conditioning" the market

Regular Release of Factual Business Information

- You can continue regular release of factual business information, such as announcements of new products, etc. You should try to continue prior ordinary course releases. If you drastically increase the amount of releases you make, the SEC may take notice.

Materials Released More Than 30 Days Before First Filing

- Statements made by a company more than 30 days prior to its first filing of its registration statement that do not reference an IPO and for which the company takes "reasonable steps to prevent further dissemination of the communication" are excepted from the general rule
- "Reasonable steps" has not been defined, but think about publication schedules, etc., for any pre-IPO statements that are made
- Any such statements should focus on products and services and not the company, prospects, any future IPO or other topics that may be appear aimed towards conditioning the market.

Section 16 Reporting

- Before pricing, all officers, directors and 5% stockholders will have to file Form 3's
- That means that you will have to get EDGAR filer numbers for each of them
- Determine whether you will acquire your own software to make these filings or rely on the financial printer.
- Short filing deadlines for Form 4's makes it important to have your process down and understood by all Section 16 reporting people and entities

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D&O and 5% Stockholder Questionnaires

- Your outside counsel will prepare very detailed questionnaires for all of your named executive officers, directors and 5% stockholders
- Often, these people will need help with the detailed compensation and option ownership questions. Often, the company will fill out the compensation and stock ownership section and ask executives to confirm the numbers in their questionnaire
- Private equity and VC funds need to identify their general partners and their managers or directors who control the shares

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SEC Comment Letters

- Letters and responses are made public after IPO completed, so there is added pressure to get it right the first time and avoid highlighting changes or issues

Conclusion

- An IPO is a very time consuming process. It is difficult for management and the general counsel to participate in the IPO process and still handle full time duties with the company. With that in mind, consider trying to get as much done prior to the kick-off meeting as possible. The more organized you are and the more you can get done up front will help out greatly later when you are trying to turn drafts of the registration statement, prepare road show presentations and deal with SEC comments.

Outside Counsel's Perspective

Understanding the Client

- If you do not already know the client well, you need to spend a fair amount of time getting up to speed on the client and their industry.
- Understand the level of "help" they desire and their cost/benefit analysis of the project. Help them understand places where they can save legal fees and places where it is unwise to do so.

Outside Counsel Interaction with Board

- Help assess Board's readiness to handle public company responsibilities
- Often attend banker bake-off
- Often an early meeting with the Board to discuss process/issues
- Often a meeting with the Board to discuss fiduciary duties and Board and committee responsibilities, go over committee charters and public company policies

Defensive Measures

- Often outside counsel will meet with Board to help them decide what defensive measures should be adopted
- Most non-controversial
- Authorization of blank check preferred stock
- No cumulative voting
- Allow Board to fill Board vacancies
- Prohibiting stockholders from acting by written consent
- Supermajority vote to revise certain charter/bylaw provisions
- Not allowing stockholders to call stockholder meetings
- Directors removed only for cause

Defensive Measures

- Classified Board
  - Less popular than in years past
  - ISS dislikes
  - Unlikely to impact IPO valuation
- Poison Pills
  - Seldom seen in today's IPOs
  - ISS strongly against
  - May impact IPO valuation

Institutional Shareholder Services Inc. "ISS"

- www.issgovernance.com
- Advises institutional investors on voting
- Annually make recommendations on issues like say-on-pay, majority voting on Board elections, defensive measures, etc.

Hot Button Issues

- The SEC, ISS and institutional shareholder activists seem to be focusing on a lot of the same issues
  - Shareholder access to proxy and ability to elect directors (SEC recently re-opened the comment period on proposals relating to shareholder director nomination proposals)
  - Executive pay (more disclosure, shareholder say-on-pay)

Outside Counsel Interaction with Compensation Committee

- Often help compensation committee develop post-IPO management compensation and Board compensation
- Typically take lead in drafting compensation disclosure
- SEC hot-button issue – they want specific disclosure around how and why management is compensated

Help Ensure Good Process in Drafting Registration Statement

- Make sure the Board is given ample opportunity to comment on draft, especially the business section and box
- Make sure operational experts given ample opportunity to comment on draft – COO, CTO, Chief Product Officer, etc.
- Help set up good disclosure committee process for IPO and beyond
- If the company has international operations, make sure FCPA, tax and other regulatory compliance issues are discussed and compliance programs are in place

Third Party Resources

- www.complianceweek.com
- www.thecorporatecounsel.net
- www.section16.net

JOBS Act

Initial Public Offering Provisions

Emerging Growth Companies

- The JOBS Act exempts Emerging Growth Companies ("EGCs") from certain requirements of going public
- EGC is defined as any company with annual gross revenues of less than $1 billion during last fiscal year

Relief for EGCs

- Allowed to "test the waters" by soliciting indications of interest before preparing a registration statement
- Provided confidential SEC review of IPO registration statement
- Fewer restrictions on research reports
- Decreased financial reporting burdens

Relief for EGCs (continued)

- Less burdensome compensation disclosure requirements
- Exempt from say-on-pay and golden parachute voting requirements

Additional Issues

- EGC status is optional
- Most companies going public will likely qualify for EGC status

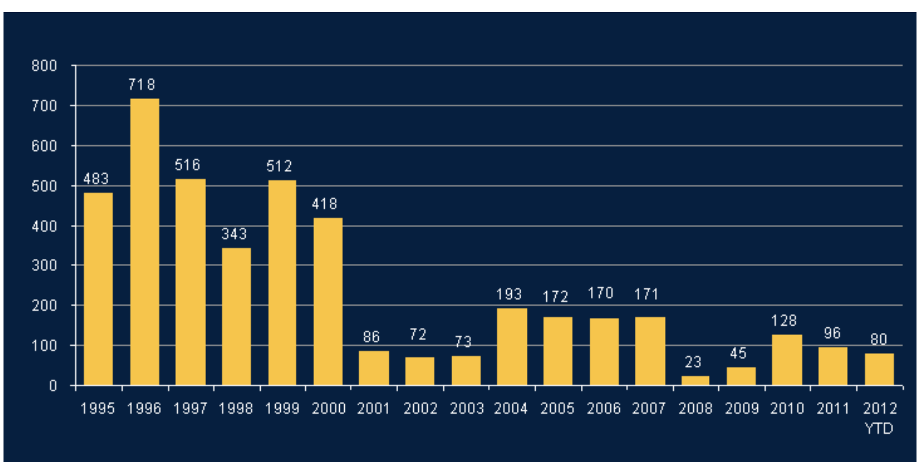
State of the Technology Equity Capital Markets

Jeff Hoffmeister

Head of East Coast Technology Investment Banking

September, 2012

IPOs Priced Annually



Last Updated
Jan. 10, 2010
PBW
Source: *Dealogic*

Source: Dealogic, Data as of August 21, 2012.

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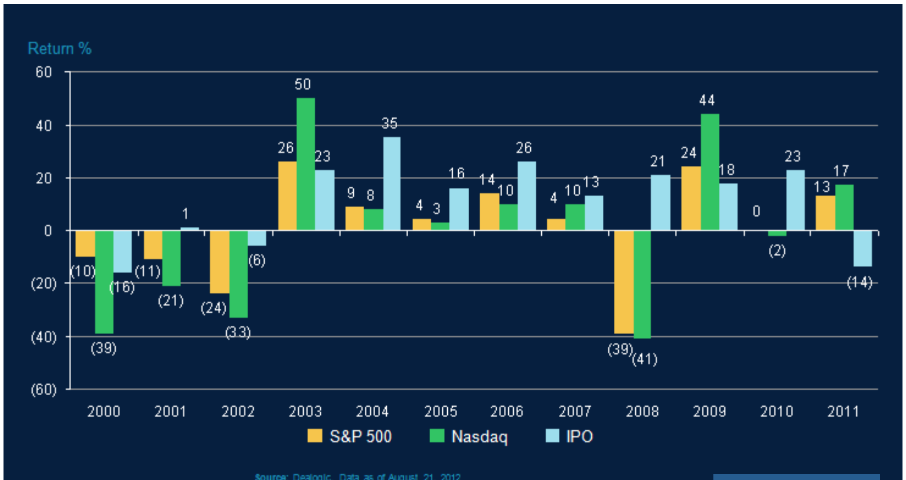
IPO Performance vs. Market



Last Updated:
January 1, 2010
PBW
Source: *Dealogic*

Note:
1. Median return as of 12/31 of respective year for IPOs priced in year.

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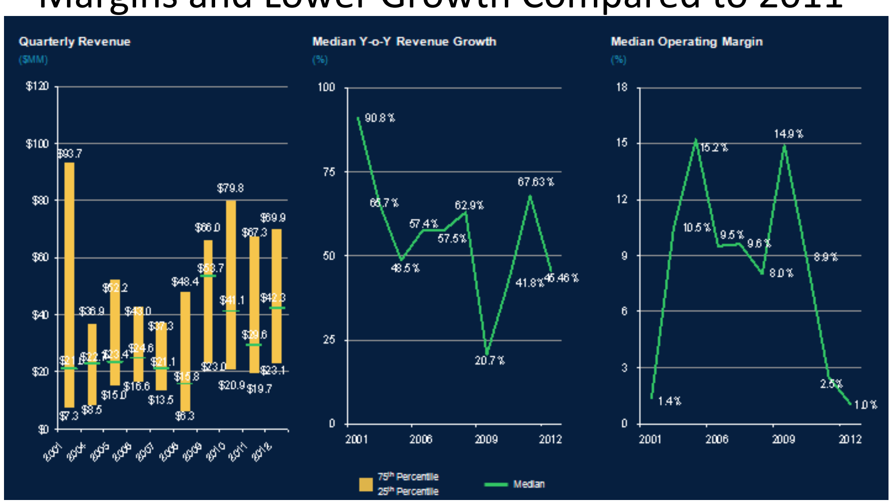
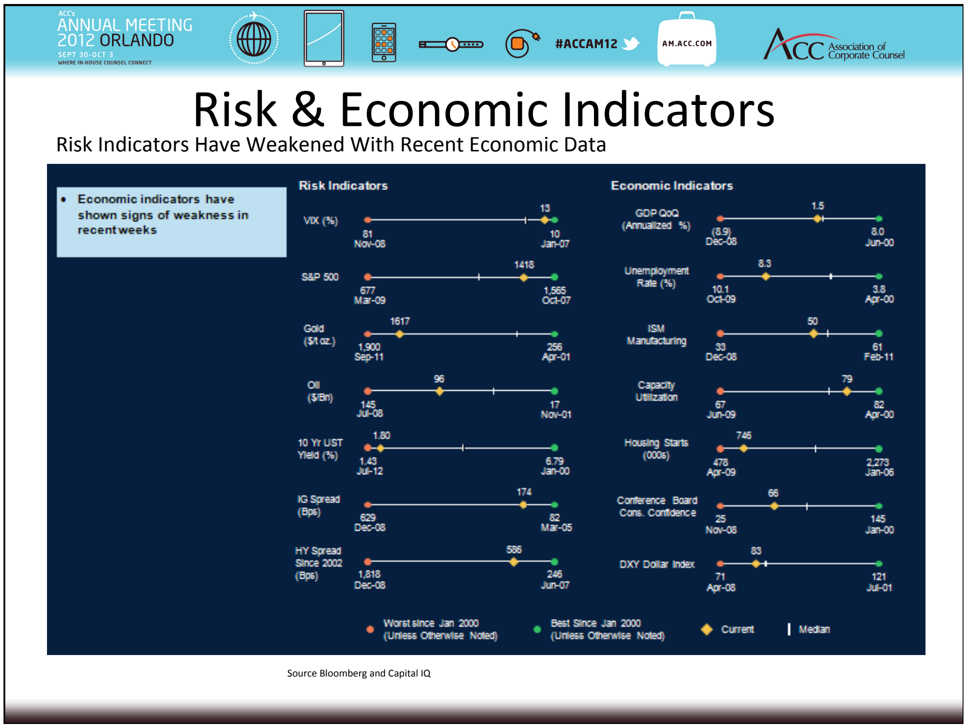
IPOs in 2012 Have Had Higher Revenues and Lower Margins and Lower Growth Compared to 2011



Note:
1. Sample of Technology IPOs. Data as of August 17, 2012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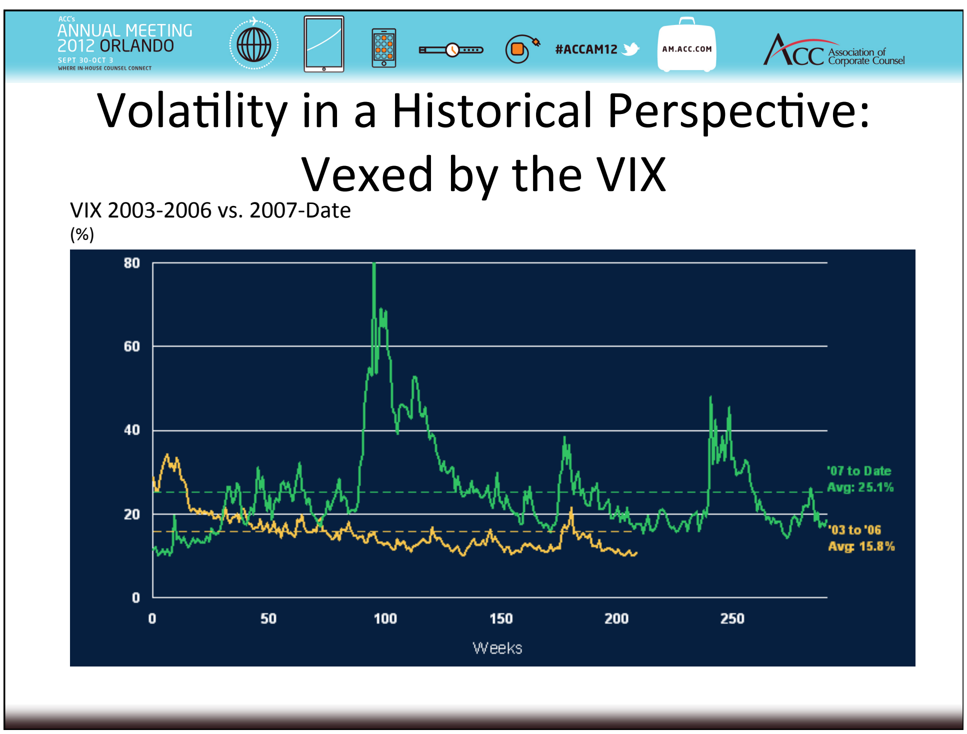
Risk & Economic Indicators
Risk Indicators Have Weakened With Recent Economic Data
• Economic indicators have shown signs of weakness in recent weeks
Risk Indicators
VIX (%) 13 81 Nov-08 10 Jan-07
S&P 500 1418 677 Mar-09 1,565 Oct-07
Gold ($/1 oz.) 1617 1,900 Sep-11 256 Apr-01
Oil ($/Brl) 96 145 Jul-08 17 Nov-01
10 Yr UST Yield (%) 1.80 1.43 Jul-12 6.79 Jan-00
IG Spread (Bps) 174 629 Dec-08 82 Mar-05
HY Spread Since 2002 (Bps) 586 1,818 Dec-08 246 Jun-07
Economic Indicators
GDP QoQ (Annualized %) 1.5 (8.9) Dec-08 8.0 Jun-00
Unemployment Rate (%) 8.3 10.1 Oct-09 3.8 Apr-00
ISM Manufacturing 50 33 Dec-08 61 Feb-11
Capacity Utilization 79 67 Jun-09 82 Apr-00
Housing Starts (000s) 746 478 Apr-09 2,273 Jan-06
Conference Board Cons. Confidence 66 25 Nov-08 145 Jan-00
DXY Dollar Index 83 71 Apr-08 121 Jul-01
Worst since Jan 2000 (Unless Otherwise Noted)
Best Since Jan 2000 (Unless Otherwise Noted)
Current
Median
Source Bloomberg and Capital IQ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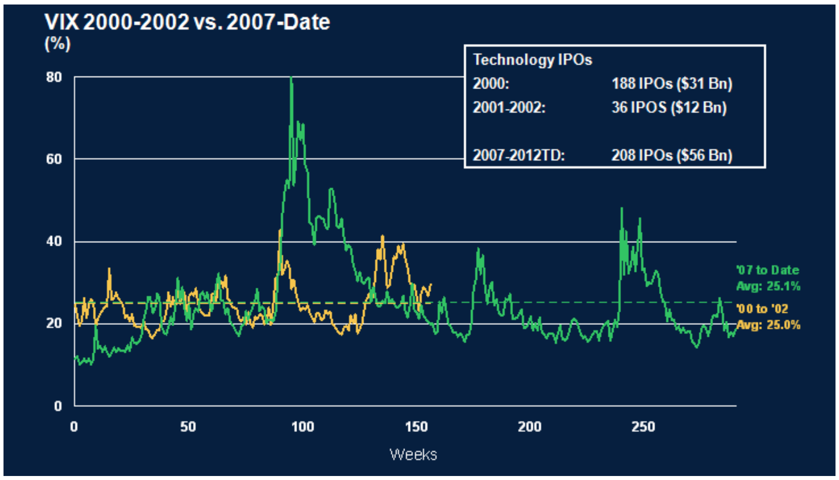
Volatility in a Historical Perspective: Vexed by the VIX
VIX 2003-2006 vs. 2007-Date
(%)
80
60
40
20
0
0
50
100
150
200
250
Weeks
'07 to Date Avg: 25.1%
'03 to '06 Avg: 15.8%

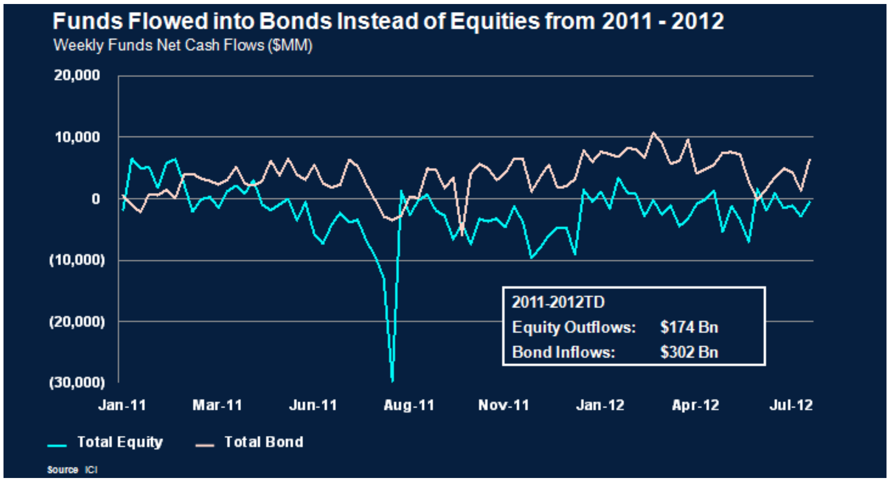
But We Have Seen This Before



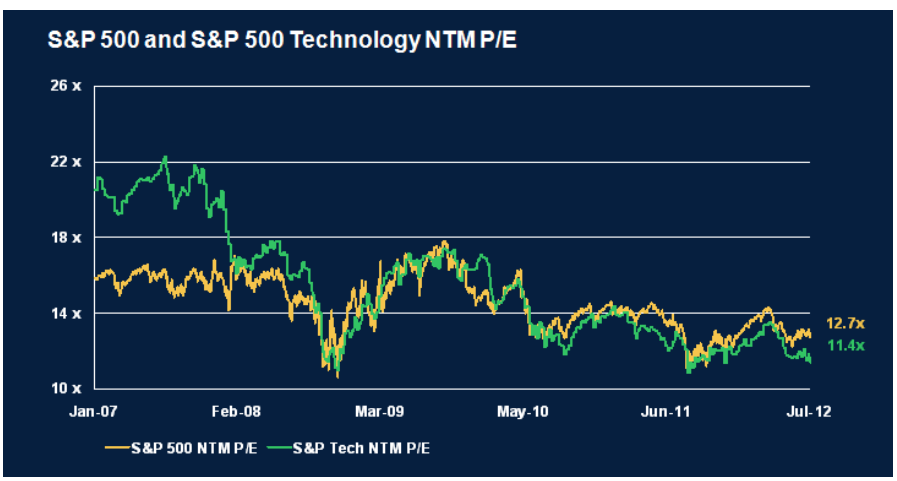
How Does Volatility Impact Investors?

- Sharp, violent price movements paralyze even the most long-term investor
- Investors leave risky asset classes for safer returns
- Valuations compress as less capital available, fundamentals are less important, and all stocks appear 100% correlated
- Investors are less willing to finance companies unless at terms where risk seems to disappear

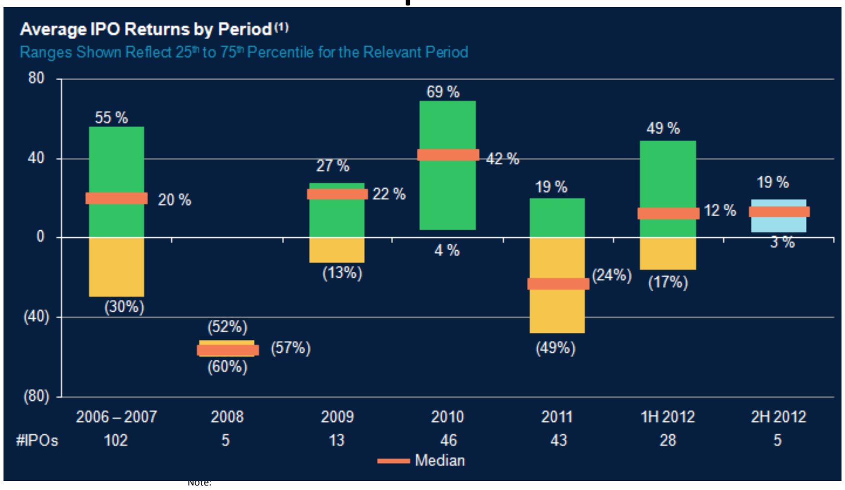
Assets Find Safest Absolute and Relative Returns



Deleveraging and Inherent Market Volatility Compress Valuations of Assets, Especially Risky Assets

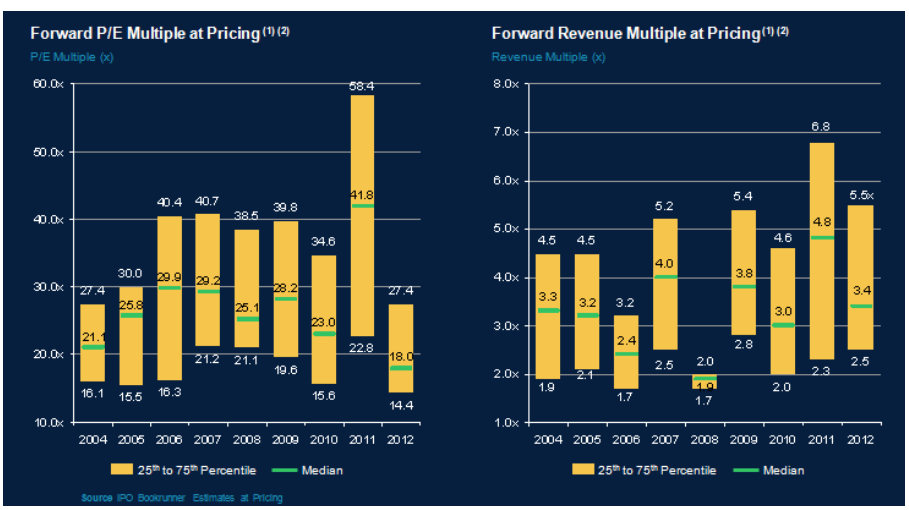


In 2012, Investors Requiring Higher Returns to Participate in IPO Market



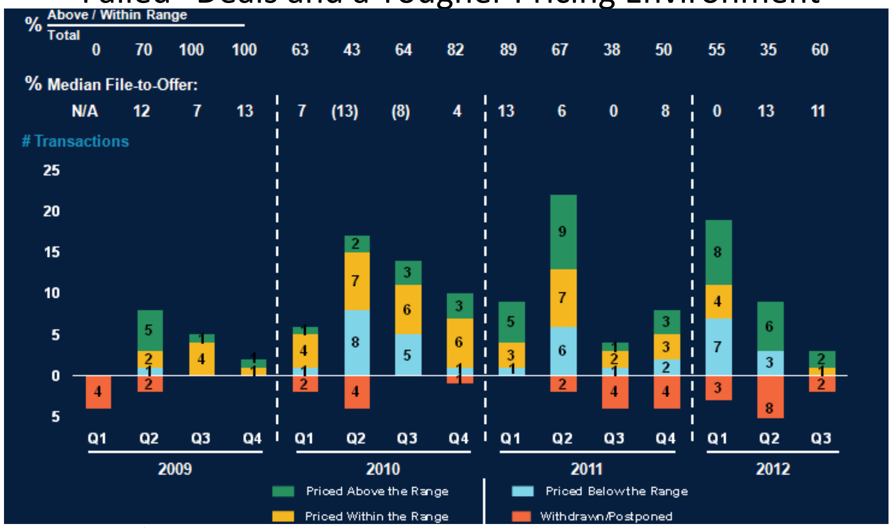
Note:
1. Return values reflect price performance between offer and December 31 of the IPO issuance year for each IPO. 2012 IPO returns are estimated based on offer to current as of August 17, 2012.

U.S. Technology IPO Valuations Over Time



Note:
1. As of August 17, 2012; includes U.S. listed technology offerings over $30 million.
2. Based on initiation of coverage reports by bookrunner post-IPO as of August 17, 2012.

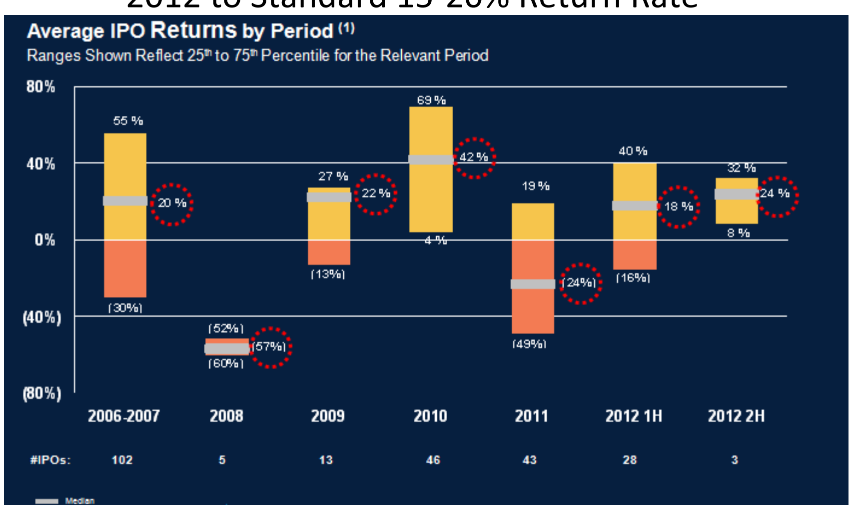
IPO Volumes Consistent with Prior Years Despite More "Failed" Deals and a Tougher Pricing Environment



Source: Dealogic

Note:
1. As of July 20, 2012
2. IPOs & Follow-ons include U.S. listed offerings over $30MM

Despite Headlines: IPO Investor Returns Have Normalized in 2012 to Standard 15-20% Return Rate



Note
1. Return values reflect price performance between offer and December 31 of the IPO issuance year for each IPO. 2012 IPO returns are estimated based on offer to current as of July 20, 2012

IPO Investors: What Has Resonated Most?

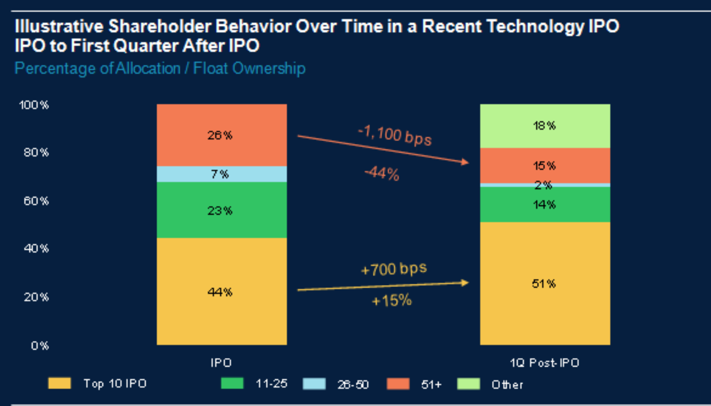
1. Premium Revenue Growth—Bankable 25% or Greater Growth
2. Conservative Street Model and Ability to Outperform the Model is Key
3. Management with Public Company Track Record—Especially ones with experience managing for growth
4. Enterprise-driven Businesses—Perceived to be less risky, more predictable and "clean" models not in transition
5. Competitive Moat—Leading Technology, dominant market share

IPO Investors: What Has Resonated Most? (cont'd)

6. Weak / Fragmented Competition—Especially good if your competition are large cap, slower growth technology companies
7. Tangible "Immediate" Large Addressable Market
8. Likely M&A Candidate of Large Cap, Investment Grade Tech Companies

IPO Investors: Top Allocations Receive Majority of Shares and Invest for the Long-Term at IPO

As a group, the top ten investors tend to increase holdings over time, and "tail investors" often sell their very small share allocations



Source: Morgan Stanley, Thomson

IPO Investors: But "Long Tail" Investors Are Crucial in Follow-ons and Future Liquidity Events

Six of the top ten follow-on investors, including the #1 investor came from outside the IPO top ten

IPO top ten investors often participate in the follow-on, but tend to comprise a lower allocation percentage

Top 10 Allocations at Follow-on

1	Mutual Fund 1	14%	51+ Allocation
2	Mutual Fund 2	11%	Top 10
3	Mutual Fund 3	8%	Top 10
4	Mutual Fund 4	8%	Top 10
5	Mutual Fund 5	7%	Top 10
6	Hedge Fund 6	6%	51+ Allocation
7	Mutual Fund 7	6%	Top 25
8	Hedge Fund 8	5%	Top 25
9	Hedge Fund 9	2%	Top 50
10	Hedge Fund 10	2%	No IPO Allocation

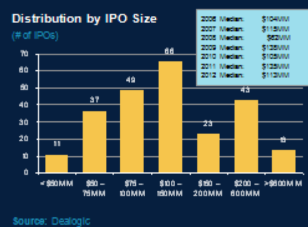
Top 10 IPO Investors 11-25 26-50 51+ Other

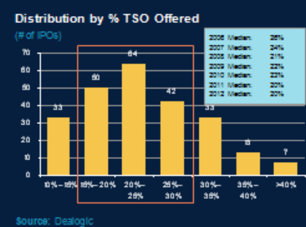
Source: Morgan Stanley

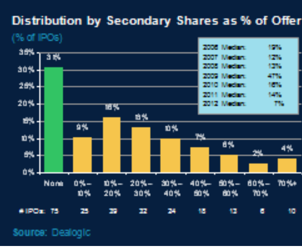
IPO Sizing and Structuring Considerations

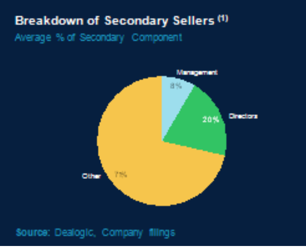
U.S. Listed Technology IPOs Since 2006 (1)

- We have analyzed all U.S. listed technology IPOs priced since 2006 (242 deals in total)
  - Typically between 15% and 30% of the companies were sold at IPO
- 69% of the technology IPOs since 2006 had a secondary component
  - The majority of the secondary selling came from non-insiders
  - Companies that went public were more mature and generated positive operating cash flows
  - Greater free float and liquidity at IPOs creates better technical conditions for future secondary sell-downs



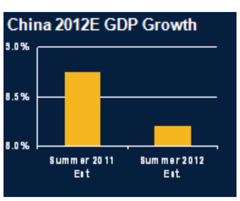






Note:
1. As of August 17, 2012; includes U.S. listed technology IPOs greater than $30MM since 2006.

So Tired of Déjà Vu …but Uncertainty Remains



China Slowdown

EU Breakup / Euro to Zero

U.S. Fiscal Cliff

Geopolitical Risk

U.S. Elections

Anemic GDP / Employment Growth

Key Conclusions on Current Level of Volatility

- Economies and markets are still living in a post-2008 world where cycles of optimism and pessimism <u>occur frequently</u>
- Consequently, investors have been conditioned to move rapidly from risk off to risk on and back again
- Less financing "market windows" more "ebbs and flows" of volumes
- We can expect volatility to persist as markets continue to be driven by macro events and news flow
- "People will look and pay for great growth assets in the stock market especially with economies looking weaker around the world"

Securities Law Advisory

July 24, 2006

The SEC's Gun-Jumping Rules: Alive and Well

While the Securities Offering Reform (Reforms)[1] liberalized many of the rules relating to communications during an offering, the Reforms did not eliminate the Securities and Exchange Commission's (SEC) "gun-jumping" rules,[2] the thrust of which are to prohibit actions and communications that condition the market in advance of a public offering. We want to remind issuers and underwriters of the role of the SEC's long standing gun-jumping rules in light of the Reforms.

What is Gun-Jumping?

Securities offerings can be divided into three stages based on the regime set forth under Section 5 of the Securities Act:

- the "quiet period," which begins with the decision to proceed with an offering and ends with the filing of the registration statement;
- the "waiting period," which is the period between the filing and effectiveness of the registration statement; and
- the "post-effective period," which is the period after the registration statement has been declared effective by the SEC.

Prior to the Reforms, oral and written offers[3] by any issuer were prohibited during the quiet period. During the waiting period, oral or written offers, but not sales, could be made, but any offers made in writing could only be made by means of a "statutory prospectus" that conformed to the information requirements of Section 10 of the Securities Act, typically a preliminary or "red herring" prospectus. Violations of these

1 Final Rule: Securities Offering Reform, Rel. Nos. 33-8591, 34-52056, IC-26993 http://www.sec.gov/rules/final/33-8591.pdf (Jul. 19, 2005). See *Alston & Bird LLP Securities Law Advisory*, "SEC Adopts New Rules Liberalizing Capital Raising Process," http://www.alston.com/articles/05-249%20SEC%20Liberalizing%20Capital%20Raising.pdf (Jul. 28, 2005)(Alston & Bird Offering Reform Advisory).

2 Traditional gun-jumping lore has developed over many years of SEC decisions and releases and centers around the interpretation of Section 5 of the Securities Act of 1933, as amended (Securities Act), and the nature and timing of permissible communications thereunder. See, e.g., *SEC v. Arvida Corp.*, 169 F. Supp. 211 (S.D.N.Y. 1958) and Guidelines for Release of Information by Issuers Whose Securities are in Registration, Rel. No. 33-5180 (Aug. 20, 1971).

3 The term "offer" includes "every attempt or offer to dispose of, or solicitation of an offer to buy," and has been broadly interpreted by the SEC to include publicity deemed to prepare or condition the market for the proposed offering.

basic restrictions generally are referred to as "gun-jumping"[4] and may result in an SEC imposed "cooling-off" period, rescission rights to purchasers in the public offering and class action or other litigation.

What was the Effect of the Reforms on Gun-Jumping?

Communication Safe Harbors

The Reforms included safe harbors for communications made more than 30 days before filing a registration statement that do not reference a securities offering[5] and for the regular release of "factual business information"[6] and "forward-looking information."[7] Codifying existing SEC positions, the SEC created these safe harbors to encourage issuers to continue to provide regularly released ordinary course communications prior to and during an offering. As a general rule, communications referencing a securities offering that is or will be the subject of a registration statement fall outside the protections of these safe harbors, and the limited notice permitted by Rule 135 continues to be the only means by which an issuer (other than a well-known seasoned issuer (WKSI)) or a selling security holder may publicly discuss an upcoming offering during the quiet period.[8]

Rule 134

Notwithstanding the Reforms' expansion of Rule 134[9] to permit a notice including a broader range of information regarding the issuer and its business, the offering,[10] and related procedural matters, the role of Rule 134 within the gun-jumping regime has not changed. Specifically, a Rule 134 communication can be made *only after an issuer has filed a registration statement*. Likewise, the expanded rule requires that if a Rule 134 communication solicits an offer to buy or requests an indication of interest, the notice also must

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4 Gun-jumping violations typically relate to the nature and timing, as opposed to the accuracy, of statements that may constitute an offer under the Securities Act. The SEC's anti-fraud provisions mandate that all offering materials – whether oral or written – must not contain material misstatements and must not omit material information necessary to make the statements made therein not misleading.

5 Prior to the Reforms, it had been the SEC's position that after an issuer held an "organizational meeting" for its securities offering (usually more than 30 days prior to filing a registration statement), it was in "registration" and subject to the gun-jumping provisions.

6 Rules 168 and 169.

7 Rule 168. Unlike the safe harbor for communication of factual business information which is available to all issuers, the safe harbor for communication of forward-looking information is only available to reporting companies.

8 A Rule 135 notice may contain only the most basic offering information including, among other things, the name of the issuer and the title, amount and basic terms of the securities offered as well as a brief statement of the manner and purpose of the offering (but not the names of the underwriters). See Rule 135.

9 See *Alston & Bird Offering Reform Advisory.*

10 A Rule 134 notice may now discuss terms of the offering including the terms of the securities being offered, information regarding underwriters, procedural information for transactions in connection with the offering, the anticipated schedule for the offering, a brief description of the use of proceeds and a description of marketing events.

be accompanied or preceded by a statutory prospectus that includes a bona fide price range and a maximum amount of securities being offered.[11]

Free Writing Prospectuses

Following the filing of a registration statement, most issuers and offering participants may use free writing prospectuses[12] (FWPs) containing information that may go beyond (but may not be inconsistent with) the substantive information in the prospectus. Since their availability in December 2005, FWPs have become popular among issuers as a means of quickly disseminating updated information about an offering without the formality and detailed disclosure requirements[13] of a prospectus supplement or potential delay involved with an amendment to the registration statement. Given the speed with which FWPs may be disseminated, issuers must be careful not to overlook the technical requirements of Rules 164 and 433.

The risks posed by FWPs have been demonstrated most recently by the well publicized problems that Vonage had in connection with the directed share program in its initial public offering. In what appears to have been a solicitation of interest from Vonage's customers, Vonage sent a mass voice mail to its customers discussing the directed share program and explaining the steps necessary for those customers to participate in the program. As noted in the adopting release in connection with the Reforms, "written communications" include broadly disseminated voice mails. Consequently, the Vonage blast voice mail may constitute a free writing prospectus that would be required to be filed with the SEC and, because Vonage is an unseasoned issuer, would need to be accompanied or preceded by a statutory prospectus.

In the event that, as it has been suggested in the media, Vonage failed to satisfy any of the technical requirements with respect to the use of a FWP, customers participating in the directed share program could potentially have the right to rescind their purchase of the shares (a significant risk given that Vonage's stock price has traded down substantially below the initial public offering price). Multiple class action lawsuits have been filed against Vonage asserting, among other things, that the offering (including the directed share program) was conducted in a defective manner with a defective prospectus in violation of the Securities Act.

WKSIs

WKSIs may, at any time *before and after* the filing of a registration statement, make oral and written offers, including through the use of a FWP. This stems from the fact that today's largest issuers are followed by sophisticated institutional and retail investors, as well as by research analysts that regularly seek new information on a continual basis. This is in sharp contrast to the pre-Reform regime in which all issuers were treated the same for purposes of the gun-jumping rules.

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11 Neither Rule 134 communications nor Rule 135 notices constitute free writing prospectuses because they are not considered to be prospectuses or offers, respectively, for purposes of the gun-jumping provisions.

12 A "free writing prospectus" generally is any "written communication" that constitutes an offer to sell or a solicitation of an offer to buy the securities relating to a registered offering that is not a statutory prospectus.

13 Other than a required legend, there are no specific line item disclosure requirements for a FWP.

Conclusion

With the exception of the favorable treatment given to WKSIs, the regime governing the dissemination of information during the offering process remains largely unchanged. Given the severe consequences of a gun-jumping violation, issuers and underwriters must maintain a disciplined approach to communications during the offering process to ensure that they are in technical compliance with the rules and are not taking actions that could be deemed to be conditioning the market. This type of discipline should help both issuers and underwriters avoid some of the pitfalls that still exist in the SEC's gun-jumping rules even after the liberalization of communications brought about by the Reforms.

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Securities Law ADVISORY

April 5, 2012

JOBS Act Aims to Jumpstart Capital Formation

Practical Considerations for Issuers and Other Market Participants

The Jumpstart Our Business Startups Act (otherwise known as the JOBS Act), which was signed into law by President Obama on April 5, 2012, contains the most sweeping set of changes to the securities laws governing public and private offerings since the Securities Offering Reform was enacted in 2005. The JOBS Act is intended to lessen in a very broad way the regulatory burdens for emerging growth companies and other issuers seeking to raise capital.

Broadly speaking, the JOBS Act is intended to encourage capital formation in the United States by facilitating:

- initial public offerings by "Emerging Growth Companies," and
- private and small unregistered public offerings by a broader class of issuers.

Among its more significant provisions, the JOBS Act:

- creates a new category of issuer, "emerging growth company" (EGC), with substantially reduced disclosure, auditing and other requirements;
- relaxes restrictions on solicitations for private offerings, permitting advertising and other forms of general solicitation so long as all of the actual purchasers of the securities are either accredited investors (for Regulation D offerings) or qualified institutional buyers (for Rule 144A offerings);
- exempts "crowdfunding" from securities registration requirements, allowing companies to raise relatively small amounts of capital through small investments from a large pool of investors;
- raises from $5 million to $50 million the exemption limit for securities issued in small unregistered public offerings; and
- raises the threshold for the number of shareholders that a company must have to be required to register a class of securities and for banks and bank holding companies to deregister their securities.

Many of the provisions of the JOBS Act instruct the Securities and Exchange Commission (SEC) to adopt implementing rules within 90 days to one year of the date of enactment. Because the SEC has not yet completed the rulemaking required by the Dodd-Frank Act, passed in 2010, it is possible that the SEC may not be able to satisfy this more aggressive timetable.

Emerging Growth Companies

The JOBS Act exempts EGCs from some of the costly requirements of going public and thereafter of being a public company (for up to as long as five years) and eliminates certain other impediments to a successful initial public offering (IPO). By so doing, the JOBS Act is intended to encourage capital formation by making the IPO process more attractive to many companies that may have previously been hesitant to go public. EGC is defined as any company that had total annual gross revenues of less than $1 billion during its last fiscal year. Generally speaking, a company continues to be an EGC until five years have passed since its IPO, the company's total gross annual revenues have reached $1 billion (indexed for inflation), the company has issued more than $1 billion in non-convertible debt in the prior three years, or the company is deemed to be a "large accelerated filer" (meaning, among other things, its public float has reached $700 million).

The substantial regulatory relief offered to EGCs includes the following:

- **EGCs are allowed to "test the waters."** An EGC, along with its authorized persons, including underwriters, is allowed to "test the waters" with qualified institutional buyers (QIBs) and institutional accredited investors before and after the initial filing of a registration statement. This enables an EGC to solicit indications of interest before incurring the substantial costs and burdens of preparing a registration statement and filing it with the SEC. Pre-road show meetings with key institutional investors will likely become a standard part of the IPO process for EGCs.

- **EGCs are provided confidential SEC review of their IPO registration statement.** An EGC is not required to publicly file its IPO registration statement but can instead submit it (as well as amendments to it) to the SEC for review on a confidential basis. This, and the ability to test the waters, permits an EGC to explore conducting an IPO without disclosing sensitive information to the market and enables the EGC to avoid any embarrassment associated with pulling an IPO should the company decide not to go through with it. However, at least 21 days prior to the start of any roadshow, the EGC must publicly file its registration statement and all accompanying amendments.

- **There are fewer restrictions on research reports and research analysts during the EGC IPO process.** Research reports from securities analysts, even those from broker-dealers participating in the IPO of an EGC, are no longer considered "offers" under Section 5 of the Securities Act of 1933. Thus, the JOBS Act permits securities analysts to release research reports about an EGC at any time, both pre-IPO and during the traditional quiet period following an IPO (although there is some reason to believe that analysts may be reluctant, at least initially, to take advantage of this flexibility pre-offering). This is expected to spur an increase in research coverage of newly public companies.

  Also as a result of the JOBS Act, securities analysts are permitted to meet with members of the EGC's management before the EGC files a registration statement and during the post-filing, pre-effective period, even if investment banking personnel and other representatives of the broker-dealer are present and/or coordinate the meetings.

  - These provisions of the JOBS Act require the SEC and the Financial Industry Regulatory Authority (FINRA) to revise some of their rules and interpretations accordingly. Also, although New York Stock Exchange (NYSE) Rule 472, which imposes restrictions on research, is not directly affected by the JOBS Act, the NYSE is likely to amend Rule 472 to conform with FINRA's changes to its research rules.

  - Research analysts still must comply with FINRA rules and interpretations that are not affected by the JOBS Act. For example, research analysts are still prohibited from participating in efforts to obtain investment banking business.

- **EGCs are entitled to substantial relief from financial reporting requirements.** An EGC is required to provide only two years, rather than three years, of audited financial statements and "management's discussion and analysis," and two years, rather than five years, of selected financial data, in its IPO registration statement. An EGC is not required to have its independent accountants audit management's assessment of the EGC's effectiveness of its internal controls, as is required under Sarbanes-Oxley Act (SOX) Section 404(b), although the EGC is still required to establish and maintain internal controls and to file the CEO and CFO SOX Section 302 certifications (which include statements regarding the status of the EGC's internal controls) with its periodic reports. This relief from SOX Section 404(b) is intended to result in significant ongoing savings to EGCs (although companies that qualify as "smaller reporting companies" are already exempt from SOX Section 404 requirements). Additionally, EGCs are not required to comply with new Generally Accepted Accounting Principles (GAAP) pronouncements applicable to public companies until they are also made applicable to private companies. (Often new or revised accounting standards will provide private companies with more lead time for compliance than public companies receive.) EGCs also are not required to comply with any future Public Company Accounting Oversight Board (PCAOB) rules mandating auditor rotation or requiring a supplement to the auditor's report providing additional information about the financial statements and the audit, nor will EGCs be compelled to comply with any other future PCAOB rules unless the SEC has expressly determined that the additional requirements are necessary.

- **EGCs are subject to less burdensome compensation disclosure requirements.** An EGC may use the smaller reporting company standard for compensation disclosures, meaning it must disclose the compensation of only its top three, rather than its top five, executive officers and is not required to provide the "compensation discussion and analysis" section in its IPO registration statement and subsequent periodic reports. An EGC also is not required to provide an analysis of the relationship between executive compensation and company financial performance or a ratio of annual CEO compensation to annual median worker pay.

- **EGCs are exempt from the say-on-pay and golden parachute voting requirements.** This exemption continues to apply to a company for either one or three years after losing its EGC status, depending on how long the company was an EGC.

So, what questions do you have about EGCs?

Q: ***What if an EGC prefers not to use EGC reporting status?***

A: EGC status is optional, for it is anticipated that some investors may expect larger EGCs to "step up" to the more stringent standards applicable to non-EGCs. A company must make a one-time, "all-in" choice when it is first required to file a registration statement or periodic report with the SEC. Companies are not allowed to pick-and-choose between two different sets of requirements.

Q: ***How many companies going public will qualify as an EGC?***

A: Only a few companies going public have annual gross revenues over $1 billion. By way of example, 41 companies went public during the first quarter of 2012, and out of those, only five would not have been covered under the definition of EGC.

Q: ***What if a company that qualifies for EGC status has already filed an IPO registration statement? Can the company still use the rules for EGCs?***

A: Whether such a company can take advantage of the rules for EGCs depends on when the first sale of its common equity securities took place. If a company has filed its IPO registration statement with the SEC but its IPO has not yet priced, or if its IPO was priced after December 8, 2011, then it is able to avail itself of the relaxed requirements applicable to EGCs. If this first sale occurred on or before December 8, 2011, then the company does not qualify as an EGC.

Q: ***What about investment firms subject to the Global Analyst Research Settlement? For example, are their analysts and investment bankers able to jointly communicate with an EGC's management?***

A: The JOBS Act does not address the restrictions of the court-ordered undertakings in the 2003 Global Analyst Research Settlement between the SEC and 12 investment banks. The JOBS Act permits joint analyst/banker communications with an EGC's management for any purpose and without a chaperone. Investment banks subject to the Global Analyst Research Settlement should consult counsel to determine if, and how, they may take advantage of this and other relief afforded to investment banks by the JOBS Act.

Though the above changes took effect immediately upon the JOBS Act's enactment, it is expected that the SEC and FINRA will issue certain implementing rules and interpretive guidance relating to EGCs at some point in the near future. As a result, EGCs may be unable to take full advantage of the JOBS Act's reforms until such rules and guidance are adopted.

Unregistered Offerings

Not all of the sweeping changes in the JOBS Act are reserved for companies qualifying as EGCs. The JOBS Act includes other reforms that are intended to encourage companies to raise capital in private offerings and in small public offerings without triggering registration requirements under the Securities Act of 1933 or the Securities Exchange Act of 1934.

- **Private offering restrictions on general solicitations are relaxed.** Advertising and other forms of general solicitation have until now been permissible only in SEC-registered offerings. The JOBS Act permits widespread advertising and other forms of "general solicitation" in private offerings pursuant to Rule 506 of Regulation D so long as the issuer takes "reasonable steps" to verify that all of the actual purchasers of the securities (not the offerees) are accredited investors. Similarly, for private offerings under Rule 144A, the seller and anyone acting on behalf of the seller must "reasonably believe" the buyer is a QIB. Whether the "reasonable steps" and "reasonably believe" standards will differ in practice is left to the SEC, which must implement these changes within 90 days of enactment of the JOBS Act.

  The JOBS Act also provides that persons who act to bring issuers and potential purchasers together for a Rule 506 offering are not required to register with the SEC as a broker or dealer if certain conditions are satisfied, including that the person may not receive any compensation, or handle any customer funds or securities, in connection with the purchase or sale of the securities.

  Practical consequences:

  - Initial purchasers or placement agents can be named in press releases for private offerings conducted in reliance on Rule 506 of Regulation D or Rule 144A.

  - A private Rule 506 offering could still be integrated with a concurrent public offering, thus requiring registration of the entire offering. In 2007, the SEC provided extremely helpful integration guidance in Securities Act Release No. 8828 (August 3, 2007) that set forth a framework for analyzing potential integration issues in the specific context of concurrent private and public offerings. The SEC explained that the key factor in such an analysis was how the investors in the private offering were solicited. The status of that guidance is now unclear as a result of the JOBS Act.

- The JOBS Act may change market practice for audited financial statements used in private placements and Rule 144A offerings. There has historically been a strong preference (but not a requirement) to include three years of audited financials in private placement and Rule 144A offering memoranda, consistent with the requirement for a registered offering. Because the JOBS Act permits EGCs to provide only two years of audited financial statements in their registration statements, market practice could move to including only two years of audited financial statements in an offering memorandum for a non-EGC issuer that is conducting a private placement or a Rule 144A offering.
- It is important to keep in mind that the issuer and other offering participants remain subject to antifraud liability for the content of any advertising or other general solicitation materials that are used in connection with the offering. This may cause some issuers to continue to observe the current restrictions on publicity, but without the concern that an inadvertent general solicitation would make a private placement unavailable.

- **Crowdfunding exemption is codified.** Crowdfunding, a topic that has been the subject of much discussion, is now expressly exempt from federal and state securities registration requirements by a new Section 4(a)(6) and Section 4A of the Securities Act of 1933. Crowdfunding is a capital raising strategy for private companies, often early stage or small companies, to raise small amounts of money, often via Internet platforms, through pooled, relatively small investments by a potentially large group of investors.

  Under the crowdfunding exemption, a company may sell unregistered securities to the public if the total amount of securities sold by the issuer, including amounts sold pursuant to the crowdfunding exemption during the preceding 12 months, does not exceed $1 million. The maximum amount that an individual in the “crowd” may invest under the crowdfunding exemption in any 12-month period will depend on each individual’s annual income or net worth but can range from $2,000 to $100,000. The issuer is not permitted to advertise the terms of the offering, except for notices that direct potential investors to a broker or funding portal (discussed below). Securities purchased pursuant to crowdfunding are subject to a one-year holding period unless resold to the issuer, to an accredited investor, to a family member or in a registered offering. Any crowdfunding effort will not be integrated into any other means an issuer may use to raise capital.

  Issuers must conduct crowdfunding activities through an SEC-registered broker or a newly created class of SEC-registered “funding portals.” “Funding portal” is defined as a person acting as an intermediary in a crowdfunding transaction between the issuer and the investor that does not, among other things, offer investment advice or recommendations; solicit purchases, sales or offers to buy the securities displayed or referenced on its website or portal; or hold, manage, possess or otherwise handle investor funds or securities.

  Any broker or funding portal in a crowdfunding transaction must:

  - register with the SEC;
  - warn investors as to the risks involved;
  - require each potential investor to answer basic questions demonstrating that such investor understands the risks of the investment, including illiquidity;
  - take measures to reduce risk of fraud, including performing a background check on the issuer’s principals and 20 percent or greater shareholders;

- provide a target offering amount and a deadline to reach that amount and ensure that a third-party custodian holds all investments until the target amount is reached;
- protect the privacy of information collected from prospective investors; and
- not have an interest in the issuer.

In addition, a company raising capital in a crowdfunding transaction must file with the SEC and provide to potential investors fairly detailed information about the issuer and the offering, including the following financial statements: (i) if raising $100,000 or less, a tax return and a financial statement certified by a principal of the company; (ii) if raising up to $500,000, financial statements that are "reviewed" by an independent accountant; and (iii) if raising more than $500,000, audited financial statements.

Furthermore, a company raising capital in a crowdfunding transaction will be required to make an annual filing with the SEC, the contents of which is to be determined by the SEC. Note that in addition to the issuing company, executives and directors will be liable for any material misstatements and omissions made to purchasers of securities issued pursuant to the crowdfunding exemption.

The SEC must issue rules necessary to implement the crowdfunding exemption within 270 days of enactment of the JOBS Act.

Q: Can any company use the crowdfunding exemption?

A: No. The crowdfunding exemption cannot be used by a public company nor an investment company (as defined by the Investment Company Act of 1940) and is only available to companies organized under the laws of a U.S. state or territory or the District of Columbia. Also, there is a "bad boy" disqualification for issuers who have been convicted of certain types of wrongdoing or who have filed a registration statement that is the subject of certain SEC proceedings or examinations or has been the subject of a stop order.

- **Exemption limit for small public offerings has been raised.** The JOBS Act requires the SEC to amend Regulation A, or to adopt a new exemption from registration similar to Regulation A, for public offerings by U.S. and Canadian non-reporting companies of up to $50 million of debt, equity or convertible debt securities in any 12-month period, up from the current Regulation A limit of $5 million in any 12-month period. Securities sold pursuant to this exemption are not restricted and therefore can be immediately resold. While issuers for such offerings may "test the waters" before filing any offering statement with the SEC, issuers are required to file audited financial statements annually with the SEC and may be subject to additional conditions that the SEC has broad discretion to impose. (Such additional conditions could include, for example, a requirement to file an offering statement with the SEC and deliver copies of it to prospective investors and a requirement to file periodic reports with the SEC.)

The JOBS Act does not specify a date by which the SEC must issue rules to implement the exemption, though it does specify that the SEC has 270 days to establish disqualification provisions.

Because many IPOs in the United States raise less than $50 million, this expanded exemption in the JOBS Act may significantly impact the number of smaller IPOs in the United States. However, the extent of such an impact will depend heavily on the up-front and on-going obligations that the SEC chooses to impose on companies that use the exemption.

Shareholder Threshold for Registration

- **Threshold for the required registration of a class of securities of a company has been raised.** The JOBS Act requires an issuer to register a class of its equity securities under the Securities Exchange Act of 1934 within 120 days after the end of its fiscal year if, on the last day of that fiscal year, it had total assets in excess of $10 million and a class of its securities is held of record by either 2,000 persons or 500 persons who are not accredited investors. (Previously, the threshold was $10 million in assets and at least 500 shareholders of record.) This increased threshold excludes shareholders who received their securities pursuant to an employee compensation plan as well as any securities received as part of the new crowdfunding exemption or the expanded Regulation A exemption. The JOBS Act does not specify a date by which the SEC must adopt implementing rules.

  Questions left for the SEC to address include how an issuer is to know whether an investor was, at the time of the person's acquisition of the securities, an accredited investor and whether the person has subsequently lost that status (including due to retirement or some other event). Also left for the SEC to determine is whether subsequent holders of securities that were originally issued pursuant to an employee compensation plan, the crowdfunding exemption or the expanded Regulation A exemption count toward the threshold.

  A similar change raises the shareholder cap applicable to banks and bank holding companies to 2,000 without further limiting the number of shareholders of record that are not accredited investors and also raises the threshold for de-registration by a bank or bank holding company from 300 shareholders of record to 1,200. The SEC must issue rules implementing these provisions applicable to banks and bank holding companies within one year after the enactment of the JOBS Act.

  These changes provide issuers, including large issuers that are not EGCs, with the flexibility to stay private for a much longer period of time and generate a much larger shareholder base before conducting an IPO. (Critics have pointed out that the ironic result may be that a JOBS Act meant to spur IPOs may actually deter them.) It is unclear what effect this change will have on the secondary trading market for shares of such large privately held companies. Because the shares of these companies are not registered under the Securities Exchange Act of 1934 and these companies therefore are not subject to the fulsome reporting requirements of the Securities Exchange Act of 1934, the securities cannot trade on established, recognized exchanges like the NYSE or Nasdaq. This will possibly lead to a class of companies with perhaps thousands of beneficial owners whose securities trade on private trading networks like SecondMarket or on non-U.S. exchanges like the London Stock Exchange's Alternative Investment Market (AIM).

  Q: ***Are shareholders who hold their securities in "street name" counted as shareholders of record?***

  A: No. The SEC's rules regarding shareholders of record remain unchanged. Beneficial holders who hold securities through brokerage firms, banks, etc. continue to not be counted as shareholders of record.

  Q: ***Given the new requirements for registration, can a company that is not a bank or a bank holding company and has less than 2,000 shareholders of record and 500 shareholders of record who are not accredited investors deregister?***

  A: Probably not. The JOBS Act expressly provided the threshold at which a bank or bank holding company could deregister (see above), thus Congress presumably intended to leave in place the 300 shareholder standard for delisting required by Rule 12g-4 for all other issuers.

Further SEC Studies

The JOBS Act requires the SEC to undertake several studies, such as the advisability of trading and quoting securities in one penny increments ("tick size" or "decimalization"), particularly for EGCs; a comprehensive analysis of Regulation S-K in order to recommend changes to facilitate the registration and reporting process for EGCs; a study of the impact of blue sky laws on Regulation A offerings; and a study of the SEC's enforcement authority under Rule 12g5-1(b)(3) to prevent circumvention of the record shareholder threshold condition for required registration of a class of securities under the Securities Exchange Act of 1934.

Conclusion

The JOBS Act is intended primarily to increase the number of IPOs and other capital formation transactions by smaller companies in the United States by relaxing regulatory requirements in order to decrease the costs and burdens of capital formation. In order to lessen the costs and burdens, however, the JOBS Act removes or weakens existing requirements and prohibitions intended to protect investors and the integrity of the capital markets. Whether or not those requirements and prohibitions were merely impediments to the formation of capital or were necessary to the protection of investors remains to be seen.

***This alert was written by* Gary J. Ross, M. Hill Jeffries, Mark I. Sokolow, Carol M. McGee, Douglas J. McClintock *and* David E. Brown, Jr.**

For more information, contact your Alston & Bird LLP attorney or one of the attorneys in the firm's Securities Group.

www.alston.com

A&B FORMBANK DOCUMENT
Last Edit Date 10/11

MEMORANDUM

TO: Board of Directors and Executive Officers
of [Name of Issuing Company]

FROM: Alston & Bird LLP

DATE: [Date]

RE: Publicity Prior to Initial Public Offering

As [Name of Issuing Company] (the "Company") begins to prepare for its initial public offering of [shares of common stock] [securities] (the "Offering"), it is important to keep in mind certain restrictions with respect to publicity, especially with regard to the timeframe including 30 days prior to filing of, and the expiration of up to 25 days following the effective date of, the registration statement for the Offering. The consequences of improper communications can be extremely disruptive to the timetable for the Offering and may result in the Securities and Exchange Commission (the “SEC”) requiring a “cooling off” period so that the effect of pre-conditioning can dissipate or requiring the Company to disclose in its prospectus the information contained in any materials made public outside the prospectus.

<u>Publicity Prior to Filing Registration Statement</u>

With certain exceptions, the federal securities laws make it unlawful for any person to offer to sell any security, through the use of a prospectus or otherwise, unless a registration statement has been filed as to that security. Accordingly, no oral or written offers may be made prior to the filing of a registration statement. The term "offer" includes "every attempt or offer to dispose of, or solicitation of an offer to buy," and can include publicity deemed to prepare or condition the market for the proposed offering. The law is designed to provide investors with full and fair disclosure of all of the information necessary to make an informed investment decision prior to a purchase of securities. Restrictions concerning the public dissemination of information are based on the belief that publicity efforts and oral or written publication of information in advance of a proposed offering, even if not expressed in terms of an offer to sell securities, can contribute to arousing public interest in a manner which is often deceptive or misleading. Thus, any pre-filing communication that can be construed as conditioning the market for an offering of securities (“gun-jumping”) will be considered an illegal "offer" to sell such securities.

Currently, the only kind of information concerning an issuer which may be disseminated prior to filing a registration statement is advertising of the character and content normally published by the Company and <u>routine</u>, <u>factual</u> communications to investors, employees, analysts and the press. Routine factual communications typically include factual information about the Company, its business or financial developments, or other aspects of its business and advertisements or other information relating to the Company’s products or services. Statements made by the Company that refer to the Offering, or to the possibility that the Offering will be made, are permitted only under regulations promulgated by the SEC. Such statements must be strictly limited to certain information specified in the SEC’s rules, including the name of the Company; the title, amount and basic terms of the securities proposed to be offered; the amount of the Offering to be made by selling shareholders; the anticipated time of the Offering; and a brief statement of the manner and purpose of the Offering (without naming the underwriters). Any statement referring to the Offering must include a conspicuous notice stating that the Offering is to be made only by means of a prospectus, and the statement must also include any legend required by state or foreign law or administrative authority. **Please contact [Insert Contact Name at Issuing Company] prior to the dissemination of any statement relating to the Offering.**

With regard to normal advertising by the Company, if the advertising is of the content and volume customarily done, legal problems should not be created even if the advertising coincides with the Offering. No form of communication, however, should contain material designed to assist in the proposed Offering. For example, representatives of the Company should not discuss the Company's future prospects, potential new markets or potential new product lines. **If the foregoing proves to be too burdensome a restriction, please contact [Insert Contact Name at Issuing Company] so that we can consider with you an approach that will satisfy the competing considerations that are at play.** The Company should not disseminate any form of projections, forecasts or opinions, especially those relating to income, revenues, asset value and earnings per share. It is permissible, however, for the Company to respond to unsolicited inquiries regarding factual matters, to continue to hold stockholder meetings as scheduled and to continue to make routine announcements to the press with respect to factual business developments (opening of a plant, receipt of a contract, etc.). However, in all such communications, the Company should exercise extreme caution to avoid creating the impression that such communication is part of the selling process, and **such communications should be a mere continuation of historical practices in dealing with the press**.

We would recommend that certain minimum measures be undertaken to promote compliance with the restrictions noted above.

- All advertising, press relations and publicity should be consistent with past practices in all respects, including volume, timing, distributees, nature, content and method;
- Any advertising and publicity that departs from the ordinary course of business in volume, timing or content should be reviewed by legal counsel;
- Any new advertising campaign or use of new advertising media should be avoided;
- Advertising should be strictly limited to standard product information directed to trade and technical audiences;
- Any advertising aimed directly or indirectly at investors rather than customers should be avoided;
- Although the Company should discourage interviews and press coverage, it should not avoid answering factual questions. Sometimes, near-total silence can indicate by implication that an offering is in process and produce market conditioning effects;
- Appearances at industry forums should be monitored closely, and no distributions of written materials or projections should be made. No oral or written information should contain predictive matter or attempt to quantify any qualitative statement;
- Records of all advertising, press relations and publicity (including expenditures) should be kept for defense against any assertion of market conditioning;
- The Company's web site should not refer, by hyperlink or otherwise, to the Offering and should avoid overly enthusiastic statements, or hype, regarding the Company's current or anticipated performance; and
- The Company should not significantly expand its web site because it could be construed as gun-jumping.

Communications During the Waiting Period

After a registration statement relating to an offering has been filed with the SEC but before it becomes effective (the "waiting period"), the issuer is permitted to publish limited information about the Offering. Such information is limited to specified items within the SEC's rules. In addition, oral offers may be made and certain statutory prospectuses (i.e., the preliminary prospectus) may be used during the waiting period.

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Similarly, the Company generally may provide further information in the form of a free writing prospectus, but it must be accompanied or preceded by the most recent statutory prospectus. A free writing prospectus may provide more or different information than that included in the statutory prospectus, but it must not conflict with the prospectus or prospectus supplement filed as part of the registration statement. A free writing prospectus generally must also be filed with the SEC. **Please contact [Insert Contact Name at Issuing Company] prior to the dissemination of any information, whether in the form of a statutory prospectus, advertisement or term sheet.**

No sales may be made, however, until the registration statement has been declared effective by the SEC.

Communications During Post-Effective Period

After the effective date of the registration stat4ement, sales of the securities can be made, provided that any confirmation is accompanied by or preceded by a final prospectus. Moreover, through the 25th day following the effective date (the conclusion about the 25th day is based on the assumption that the Company's common stock will be listed on a registered national securities exchange or the Nasdaq Stock Market's National Market), any dealers effecting transactions in the securities may be required to deliver a final prospectus to such purchasers. The Company should also continue its restrictive policies with respect to the release of information prior to the 25th day following the effective date, as any announcements could constitute a prospectus not meeting the statutory requirements.

After the completion of the Offering, as a public company, the Company will have to remain vigilant with respect to its communications with the public and particularly with securities analysts. Issues such as pre-publication entanglement (i.e., where the Company provides information to analysts for use in their reports) and post-publication adoption (i.e., where the Company is deemed to have adopted certain information by distributing analysts reports) will become important. The Company should also consider evaluating its web site from a securities compliance standpoint. For example, the Company may want to add warning screens when users leave the Company’s web site to go to third party sites. Additionally, the Company should consider whether all information on the Company’s web site is clearly dated and whether statements cautioning users of exposure to outdated information should be added.

We hope that this information will be useful to you in evaluating your responsibilities under the securities laws. It is important that the Company take steps to inform appropriate Company personnel of the restrictions on communications described in this letter and establish procedures for the advance review of communications that present a risk of violating these restrictions. If you have any questions or comments about this letter or with respect to a proposed communication, please feel free to call [Insert Contact Name at A&B] at (404) 881-[______].

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Project IPO

January 1, 2013

[COMPANY] [UNDERWRITERS]

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Project IPO

January 1, 2013

[COMPANY] [UNDERWRITERS]

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2. **Offering Summary**
3. **Transaction Timeline**
4. **Transaction Discussion**
5. **Due Diligence List Review**
6. **Working Group List and Contact Protocol**
7. **Next Meetings**

Project IPO

January 1, 2013

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Proposed Offering Structure

Issuer:	
Size:	
Shares:	
Overallotment:	
Use of Proceeds:	
Underwriting Team **Joint Lead-Managers and Joint Bookrunners:** **Co-Manager(s):**	
Distribution Target:	
Gross Spread	
Lock-Up Period:	
Listing:	
Counsel **Company:** **Underwriters:**	
Accountants:	
Printers:	

[COMPANY] [UNDERWRITERS]

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January 1, 2013

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Transaction Timeline

January						2013
S	M	T	W	T	F	S
		1	2	3	4	5
6	7	8	9	10	11	12
13	14	15	16	17	18	19
20	21	22	23	24	25	26
27	28	29	30	31		

February						2013
S	M	T	W	T	F	S
					1	2
3	4	5	6	7	8	9
10	11	12	13	14	15	16
17	18	19	20	21	22	23
24	25	26	27	28		

March						2013
S	M	T	W	T	F	S
					1	2
3	4	5	6	7	8	9
10	11	12	13	14	15	16
17	18	19	20	21	22	23
24	25	26	27	28	29	30
31						

April						2013
S	M	T	W	T	F	S
	1	2	3	4	5	6
7	8	9	10	11	12	13
14	15	16	17	18	19	20
21	22	23	24	25	26	27
28	29	30				

Week 1	• Telephonic organizational meeting	All
	• Begin business and legal due diligence	All
	• Distribute initial draft of prospectus	CC, Company, UW
	• Drafting session in Las Vegas, NV	All
Week 2	• Due diligence calls	UW
	• Distribute second draft of prospectus	CC, Company, UW
	• Distribute draft of underwriting agreement	UC
	• Distribute draft of lock-up agreement	UC
	• Distribute draft of comfort letter	UC
	• Drafting session in Las Vegas, NV	All
	• Management presentation to research analysts	Company
	• Submit prospectus to A National Office	A
Week 3	• Finalize prospectus	All
	• File prospectus with SEC	Company, UC
	• Issue press release announcing filing	Company
Week 4	• Commence drafting of roadshow presentation	UW, Company
Week 6	• Finalize roadshow presentation	UW, Company
Week 7	• Receive SEC comments	Company, CC
Week 8	• File Amendment No. 1	All
Week 9	• Receive SEC comments	Company, CC
Week 10	• File Amendment No. 2	All
Week 11	• Receive SEC comments	Company, CC
	• Finalize underwriting agreement	Company, CC, UW, UC
	• Finalize lock-up agreement	UC, Company
	• Finalize comfort letter	UW, UC, A
	• Print/circulate "red herring" prospectus	Company, UW
	• Roadshow presentation dry runs	Company, UW
Week 12	• Analyst "teach-in"/Management presentation to underwriters' salesforce	Company, UW, CO
	• Commence roadshow	Company, UW
Week 13	• Complete roadshow	Company, UW
	• Bring down due diligence	All
	• Pricing	Company, UW
Week 14	• Closing (T+3)	All
	• File final prospectus	All

Responsibility Codes

- Company = Company
- CC = Company Counsel
- UW = Underwriter
- UC = Underwriters' Counsel
- CO = Co-Managers
- A = Auditors

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January 1, 2013

[COMPANY] [UNDERWRITERS]

Transaction Overview

I. Transaction Timeline Overview

A. Due diligence
1. Company presentation to underwriters
2. Financials
3. Legal
4. Accounting
5. Segment reporting
6. Site visits
7. Key customer calls
8. Research analyst presentations and due diligence

B. Prospectus drafting sessions
1. Timing and location

C. Commitment Committee approvals

D. Transaction timing
1. Targeted filing date
2. Press release and transaction announcement
3. Salesforce presentations
4. Roadshow
5. Board approvals/pricing committee
6. Bringdown due diligence
7. Pricing and closing

II. Management Issues

A. Directors' and officers' insurance

B. Indemnification agreements

C. Actions related to the offering
1. Preparation of resolutions and appropriate authorizations
2. Authorization of additional common shares
3. Directors' and officers' questionnaires
4. Filing of registration statement
5. Pricing committee

III. Accounting Issues

A. Timing of unaudited quarterly financials

B. Comfort letter

IV. Legal Issues

A. Charter and by-laws
B. Outstanding claims/litigation
C. Other disclosure issues
  1. Regulatory issues
  2. Change of control/material change in ownership consents
D. Underwriting agreement
E. Lock-up agreements

V. Publicity

A. Pre- and post-filing period; pre- and post-effective period
B. Review of "gun jumping" rules
C. Use of free writing prospectuses; underwriter vs. issuer
D. Pending newspaper articles or other media interviews
E. Upcoming trade shows/conferences
F. Press releases (filing and others)
G. Other scheduled corporate announcements
H. Communications with employees
I. Internet sites maintained by the Company

VI. Printing of Documents

A. Selection of printer
B. Artwork for inside cover and logos
C. Transfer agent/registrar

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Due Diligence Review

I. Company and Strategy Overview

- Company history
- Organizational structure
  - Changes in corporate structure over the last **[ten]** years
- Anticipated changes as a public company
- Senior management
  - Key employment agreements
  - Key unfilled positions
  - Compensation structure and experience profile
    - Review incentive compensation plans, including planned stock/option grids
- Board composition
- Growth strategy and mission
  - Near-term objectives
  - Long-term outlook and strategy

II. Product Overview

- See Product Grid for discussion of current products
- Detail on each of Company's products with Product Sales segment
- Detail on Rental and Used Rental Equipment Sales segments
- New product pipeline
  - Milestones and timeline to launch

III. Industry Overview

- Industry segmentation
  - Commercial construction
  - Infrastructure
- Size by segment
- Growth by segment (historical and projected)
  - Associated drivers
- Competitors by segment
- Market position
- Basis of competition (price, quality, reputation, longstanding relationships, etc.)
- Barriers to entry

IV. Business Operations Overview

- Suppliers
  - Primary raw materials
  - Supplier concentration
  - Exposure to commodity price swings (ability to pass along increases)
  - Hedging techniques
- Manufacturing
  - Facilities
  - Processes
  - Quality control
- Distribution
  - Facilities
  - Relationship with manufacturing facilities
- Customers
  - Number / concentration
  - End user vs. resale
  - Average length of relationship
  - Recent noteworthy wins / losses
  - Contracts
- Sales and marketing
  - Overall strategy
  - New initiatives
  - Structure of sales and marketing organization
- Management and employees
  - Personnel by function
  - Recent hires
  - Turnover rate by function
  - Union / non-union
- Legal
  - Outstanding or anticipated litigation
  - Past material litigation

V. Turnaround Initiatives

- By function
  - Manufacturing / operations

- Sales and marketing

- Senior management

- Finance

- Noteworthy results

VI. Financial (part of separate financial due diligence call)

- Capital structure

  - Capital structure post offering

  - Ownership summary

  - Options summary including beneficiaries of all plans

- Review of financial results for the last three years (2009 – 2012)
- Review of current results against forecast
- Factors affecting revenue growth and/or timing
- Discussion of expected results by quarter for fiscal 2012, 2013

  - Discuss budgeting process

  - Discuss longer term growth assumptions

- PP&E breakdown by asset class

  - Average age of asset class

- Capital expenditures

  - Maintenance / growth requirements going forward -

  Accounting for rented equipment / sales

- A/R aging

  - Typical (by category)

- A/P Aging

  - Typical

VII. Document requests

- Financial information

  - Quarterly financial projections 2013 – 2015

    - Full income statements, balance sheets and cash flow information

    - Other major assumptions underlying projections

    - Supporting detail to projections (by customer, by SKU, bottom-up, etc.)

  - Budget vs. actual, last 3 years

  - Breakdown of cost of goods sold and operating expenses

  - Capital expenditures

  - List of unusual charges to operations

- List of non-operating assets (if any)

- Regulatory, legal
  - Key supplier agreements
  - Key customer agreements
- General information
  - Business plan, if available
  - Company presentations
  - Internally prepared peer comparison data, if available
  - Marketing materials / brochure
  - Industry reports
- Management / Personnel
  - Organizational chart
  - Employee breakdown by function
  - New employment agreements
- Capital structure
  - List of all shareholders including all options, warrants, rights and other dilutive securities
  - Schedule of financing history for equity interests, warranty and debt
    - Date, investors, dollar amounts, percentage ownership, current basis for each round and implied valuation
    - Existing debt agreements
- Intellectual property
  - List of patents, trademarks, copyrights, (if any) and expiration dates
  - Other methods (if any) employed by the Company to protect IP

VIII. Other

- Environmental liability issues
- Financial agreements (loans, etc) with officers and directors
- Length of professional relationships
  - Attorney
  - Accounting firm
  - Public relations
- External due diligence calls
  - Litigation
  - Accountants

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Please submit any changes to ____________________

Project IPO

January 2013

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What Happens On Facebook Stays On Facebook

Law360, New York (June 07, 2012, 1:05 PM ET) -- The long-standing presumption under U.S. employment law that there is virtually no protection for personal communications in the workplace is being turned on its head by a new law. This has set off a chain reaction that could transform the way U.S. businesses are required to treat such information as well as the overall employee/employer relationship involving electronic communications.

If you have been asked at one time or another by a current or prospective employer for your personal passwords to a social media or personal email account like Facebook, Gmail, etc., that will not happen again, at least in Maryland.

As an employer outside of Maryland, the practice of asking for passwords to social media sites for current or prospective employees is now under attack in every state.

On May 2, 2012, the governor of Maryland signed into law groundbreaking legislation. In essence, the law, set to go into effect in October 2012, forbids employers from asking their employees or even applicants to reveal their passwords to whatever social media or communication websites that they may use.

California, Illinois, New Jersey and Ohio have bills under consideration and in some cases waiting to be signed into law, with more states jumping on the bandwagon every day.

And now, the U.S. Congress has waded into the issue with its own bill, sponsored by Democratic lawmakers, called the Password Protection Act. The U.S. Senate version of the bill provides even broader protection extending to smartphones, personal email accounts and information on a personal computer.

Previously in Maryland, and currently in all other states, the authority of employers to obtain such information was not in doubt, and in fact it had become common practice for many employers to require turning over passwords in order to do background checks or monitor current online behavior.

But the real issue is much broader than passwords and goes to the heart of radical changes in the way we communicate and whether, as the new law suggests, an individual has an underlying right to privacy for personal communications in the workplace.

The Big Data Revolution and Privacy

Adding to the challenge of redefining privacy in the workplace, American businesses are grappling with an unprecedented explosion of data. For the first time, in 2010, the amount of data created exceeded one zettabyte, or the equivalent of one trillion (1,000,000,000,000) gigabytes — in terms most lawyers trained in the 20th century can relate to, one gigabyte of email or electronic documents can equal the equivalent 75,000 to 100,000 pages.[1] You can do the math.

Most significantly, from the business perspective, it is estimated that as much as 85 percent of this data passes through or is controlled by corporate entities at some time in its lifecycle.[2] When you hear people use the trendy phrase "Big Data," now you will have a sense of what they are talking about.

Some of this data explosion is attributable to the myriad ways that people communicate digitally and the platforms and devices they use to do it. There are over 900 million Facebook users as of March 2012, and the number is estimated to grow to one billion by the end of the year — something like 1 in 7 people on earth.

Now add in text and instant messaging, Twitter and so on — there are hundreds if not thousands of social media platforms, with new ones created all the time.

What are the privacy implications for employers and employees in this brave new digital world? To say the lines are blurring does not do it justice. Companies in the business of processing and analyzing massive amounts of data such as Facebook, Yahoo! and Google have had to develop new technology to deal with the size of data involved. Companies and organizations dealing with the fallout are still trying to figure out what they have and how to manage all the data for legal, regulatory and business purposes.

Now, add one more wrinkle — the distinction between workplace and personal devices. An easy and natural distinction has evolved between devices — cell phones, smartphones, Droids, iPods, iPads — that are purchased and used by an individual and whatever devices are provided by an employer to an employee as part of the equipment needed to do the job.

Sounds simple and straight forward enough. The problem is that in actual practice, many people are not particularly picky about what devices are used for what purpose. It is not uncommon to set up a personal iPhone to get access to work email accounts. Or for people to access their email or social media sites from work-provided devices.

The reality is that the specific devices used to access different digital communications platforms are becoming more and more interchangeable, and, to the user, almost irrelevant.

Rather than existing on the smartphone, tablet or computer, for example, the communications are processed, transmitted and stored by huge collections of servers owned or controlled by the social media service providers themselves.

The messages, pictures and other information primarily exist in the "cloud," another trendy techie phrase, not on the particular device one uses to access or modify it. That does not mean there is no data on the device itself — there often is — but the social media platforms are becoming more and more device-independent, and the bulk of the information is maintained and processed outside the device or the employer’s network.

A Possible Paradigm Shift

What does all this have to do with workplace privacy and the Maryland password law? The approach in the U.S. to workplace privacy has, for the most part, been a laissez faire, self-regulation approach operating under the general presumption that in the workplace, employees do not have an expectation of privacy.

Communications, keystrokes and other forms of monitoring by employers of employees are generally allowed and practiced with regularity. The proposed federal legislation would create a uniform national policy and move away from the current self-regulation or even a state-by-state approach.

This is the exact opposite of the approach taken by countries in Europe. Protection of personal information has been of prime importance for decades, with strict rules and limitation on access and use imposed both by individual countries and, since 1995, by the European Union itself.[3]

The origins of this highly protective attitude are generally believed to be based on a reaction to the use of information in identifying and persecuting individuals by fascist and totalitarian regimes before and during World War II.

This approach and the resulting hurdles created to screen for personal data has a tremendous impact in terms of time and cost when seeking information from companies operating in Europe in response to U.S. litigation demands or regulatory inquiries. There are strict penalties for improperly accessing, viewing or transferring personal information, even if it is intermingled with business communications.

A further complexity is that the global nature of social media communications means that sourcing a given communication to a specific country or even continent is not always a simple proposition. This would argue in favor of adopting a more unified philosophy on communication privacy one way or the other.

The underlying logic of the Maryland law, as well as the bill under consideration in the U.S. Congress and the individual state laws, is a step in the direction of a content-based rather than source-based approach to privacy.

Put another way, the law seems to imply a bright line distinction between personal, i.e., private, and work-related communication more akin to the approach taken in Europe versus the U.S.'s presumption of little or no privacy.

The new legislation does not make a distinction based on what device is used to access or create the personal information. In other words, the nature of the material itself — personal information created on a social media site and the passwords required to access it — is the key determinant of whether it can be accessed rather than where or how it is created.

If this trend continues, over time, the legal approach to managing communication in the workplace will be revolutionized, and the technological and financial implications to U.S. business could be as transformative as the evolution of the law itself.

--By Thomas I. Barnett, Stroz Friedberg, LLC

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[1] International Data Corporation, 2011 Digital Universe Study.

[2] Ibid.

[3] Data Protection Directive, Directive 95/46/EC of the European Parliament and of the Council of 24 October 1995; and Directive 2002/58/EC (addressing privacy and electronic communications).

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THE RECORDER

Privacy Laws Cause Discovery Woes

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Membership in social media apparently has its privileges. But could protecting employee passwords turn out to be a pricey proposition for employers when it comes to e-discovery?

A new law was passed in Maryland preventing employers from requiring current and prospective employees to disclose passwords and user names to online social media and communications sites — a practice until now allowed in every state.

Now the idea has gone viral. Legislation is pending in a number of states including California, and the U.S. House and Senate have their own versions. The Senate bill, named the Password Protection Act of 2012, goes even further, protecting smartphones, personal email accounts and information on a personal computer.

California's entry into the fray, Senate Bill 1349, authored by state Senator Leland Yee, D-San Francisco, passed by a vote of 28-5. This version adds yet another twist protecting students at private and public colleges and universities from disclosing their passwords as part of the application process.

THE LAW OF UNINTENDED CONSEQUENCES

When it comes to the expectation of workplace privacy for personal communications, state and federal employment law has been fairly consistent — there isn't any. The general rule has been a laissez-faire self-regulation approach in which everything from keystrokes to emails to texts can be accessed without prior notice to or consent from employees if done on company equipment.

Civil discovery in the U.S. is broad, liberal and expansive — intentionally so. Broad discovery was seen as a way to save cost and time, not increase it, when the Federal Rules of Civil Procedure, upon which most state civil procedure rules are based, went into effect. The idea was that full and open disclosure would promote earlier settlement and avoid game-changing surprises at trial — typically the most expensive phase of any lawsuit. The rule was and is simple, a party must turn over everything requested that is responsive and not privileged.

Sounds good, so what's the problem? The problem is that the FRCP was put into effect in 1938. TV was the next big thing in technology. Document discovery meant bankers boxes filled with paper. No email, no texts, no voice mail, no multiple redundant disaster recovery backup tapes with millions and millions of files, much of it duplicative.

IT'S NOT THE SAME ALL OVER

But not everyone took the same approach to discovery. In Europe for example, in the years leading up to and including World War II, fascist and totalitarian regimes used personal information to find, persecute and sometimes kill people. This legacy has been a powerful force in shaping privacy laws both in individual countries in Europe, and since 1995, in the EU as a whole, with the passage of the European Union Protection Directive and Directive on Privacy and Electronic Communications (1995 and 2002, respectively). Under these rules, getting access to purely case-related information often involves costly and extended legal battles with regulators sometimes requiring screening of individual communications by an employee under the benevolent eye of a government official.

The difference for parties whose cases originate within the EU as opposed to the U.S. is that they do not have broad, liberal inclusive discovery — quite the opposite. The general practice in the EU is more akin to the U.S. approach to arbitration. The parties agree to exchange the key documents in the matter — nothing more, nothing less. Thus, except in situations where the case itself involves some kind of personal communication, the issue of sorting through vast amounts of chaff in search of important wheat rarely arises.

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THE TIMES THEY ARE A-CHANGIN'

Adding to the complexity under the U.S. discovery model is an unprecedented explosion of data. In 2010, the amount of data created exceeded one zettabyte, or the equivalent of 1 trillion (1,000,000,000,000) gigabytes — at 75,000 to 100,000 page equivalent of email and documents per gigabyte the numbers are staggering. That number is expected to double every two years. That's big data by any measure.

Where is all this data coming from? Some of it is the result of the proliferation of social media. It is estimated that by the end of the 2012, 1 in 7 people on earth will be members of Facebook. That's a lot of friending. Add into the mix Twitter, text and instant messaging — there is a long list with new ones created every day.

But it's not only the sheer amount of data that is concerning from a data management perspective. What should worry companies, already struggling to get their arms around their own corporate information, is that nearly 85 percent of this zettabyte of data is at some point controlled or passes through corporate entities.

BREAKING DOWN THE WALLS

What does all this mean for privacy in the face of this Big Bang in the digital universe? It's not that the line between business and personal data is difficult to draw. Practically speaking, there is no line. In the past a natural division arose between personal and company supplied equipment. Anything done on your personal device was yours and anything done on a company device — business or personal — was the company's. In the world of smartphones, netbooks, notebooks and tablets, the fine distinction between business and personal equipment is honored more in the breach than in the observance.

In short, the days are numbered for the quaint distinction between personal and workplace devices. It is common for people to have their work email downloaded to their smartphones. Likewise, accessing social media sites and sending text or instant messages from work devices is commonplace. For many users the device is almost irrelevant. There is an inherent logic to that perception. In large measure, the data exists not on the device itself or even in the employer's network, instead, it is transmitted and stored in the cloud by massive collections of servers owned or controlled by the social media or messaging service providers themselves. Even identifying where a given communication actually comes from can be difficult — as amateur and professional hackers know well.

The new password protection laws create a whole new class of protected material based on the content of that material — personal data — not based on the device on which it originates or where a person physically is when the data is created or accessed. Like it or not, this is a groundbreaking step for U.S. workplace privacy law. But this exact approach has been the status quo for decades in the EU and its constituent countries.

DANGEROUS LIAISONS

What happens when you take a highly restrictive approach to the privacy of personal data in the workplace and combine it with a broad liberal approach to document discovery? Ask anyone who has tried to get data from an EU country based on a U.S. civil discovery demand. It's not a match made in heaven. The time, complexity and, as a result, the costs, can quickly soar. Requesting parties in the U.S. are used to getting most of what they think is coming to them in a timely manner. And judges with full dockets and crowded calendars are not likely to be particularly patient or interested in the nuances of French blocking statutes, the Hague Convention or EU Directives.

Under the EU model, tremendous deference to the privacy of personal information works well in an environment where the expectation for discovery is narrow and highly focused. In the U.S., while there are many critics of the current document discovery model and its effects, having little or no restrictions on personal data in the workplace is logically and practically consistent with the liberal approach of the FRCP and its state-based equivalents. While documents subject to attorney client privilege and work product protection are content based distinctions, such material is by definition limited to certain very specific types of communications and typically involve a small subset of people in a large litigation. Anyone at a company can engage in communications with other employees or outsiders that could be considered personal.

The new laws protecting the privacy of personal media passwords may be a small step in themselves. But they are a step squarely in the direction of a content based distinction and protection for personal communications and data. It seems likely that technological advancements, sensitivity to privacy, user habits and expectations will continue to support and promote the legislative trend in the U.S. toward a content-based approach to privacy. If there is no concurrent adjustment or modification to the extremely broad and unfettered approach to document discovery, the increase in time, complexity and the overall cost of discovery for U.S. litigants could be staggering.