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Good Company

Understanding New Hampshire Securities Law: How Recent Amendments May Affect Your Company's Ability to Raise Capital

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The consequences of selling unregistered securities can be harsh—regulatory proceedings, fines, and rescission of sales. Future investors are also likely to be deterred from contributing capital to a company that runs afoul of registration requirements. Registration, however, is an expensive and lengthy process, making its exceptions particularly attractive to companies seeking capital. These exceptions, which must be secured under both state and federal law, come in two forms: exemptions and, at the state-level, preemption. Recent changes to New Hampshire law expand the state's exemptions from registration in important ways, and modify the requirements for sales that qualify for preemption.

Exemptions

New Hampshire law provides for two important exemptions for start-ups and emerging companies seeking to raise funds: the exemption for pre-incorporation subscriptions, and the isolated sales exemption. The exemption for pre-incorporation subscriptions permits New Hampshire companies to sell securities to up to ten investors if all of the sales are completed within 60 days of the company's inception. The isolated sales exemption allows a company to make up to ten sales in any 12-month window, and no more than 25 sales over the life of the company. Prior to the amendment to the isolated sales exemption, issuers were limited to five sales within any 12-month window with no lifetime limit.

The benefits of allowing an increased number of isolated sales are straightforward. Companies seeking early-stage financing now have greater flexibility under state law to attract funds from a wider range of investors. As importantly, companies that unwittingly make sales that otherwise would have exceeded the limits of the pre-amendment exemption, may now avoid costly state enforcement actions and regulatory penalties. Companies that issue securities, however, should carefully track the number of sales made under this exemption on a rolling basis in the previous 12 months and since inception to ensure that the statutory limits are not exceeded.

Preemption

Exemptions are only part of the regulatory landscape. If sales meet the requirements for the federal exemption under Rule 506 of Regulation D, a company may bypass the state-level exemption scheme because federal law preempts state securities law for these sales. But a company relying on Rule 506 does not entirely avoid the state regulatory thicket as states retain the power to impose and administer fees and fines. In fact, House Bill 889-FN, which Governor Lynch recently signed into law, requires



issuers that rely on Rule 506 at the federal level to elect the federal preemption by notice filing with the state.

Notice filing includes providing a copy of the company's federally filed forms to the state and completing an abbreviated application for licensure as an issuer dealer, both within 15 days of the first sale of the offering. Late notice filers, rather than being subject to regulatory proceedings as they were previously, are now penalized \$500 for filing up to 90 days late, and \$1,000 within one year of the first sale. Issuers should also note that filing fees for notice filings are high (\$500 in New Hampshire, recurring annually), particularly if filings are made in several states.

By requiring companies to notice file for Rule 506 sales, the state provides issuers with a clear process for compliance, but limits their flexibility to interchange federal and state exemptions for the same sale. For example, a company using the Rule 506 exemption under federal law could not rely on the isolated sales exemption in New Hampshire for that transaction; instead, the amended law requires the company to elect the preemption and notice file with the state.

Calculation of Isolated Sales

New Hampshire law now excludes from the isolated sales calculation those sales made under federal preemption or another exemption (excluding the exemption for pre-incorporation subscriptions). This change allows companies which exhaust their allotted 25 isolated sales to receive later-stage financing through, for example, a Rule 506 offering and corresponding notice filing in New Hampshire. In practice, this provision enables companies that have obtained initial funds from family and friends to raise additional capital from more sophisticated investors without jeopardizing their earlier financing.

Conclusion

While the exemptions under New Hampshire law have expanded to the benefit of companies seeking capital, these gains have been offset to a degree by the new notice filing requirements. And considering the changes in a broader context, the interplay between federal and state securities law continues to pose real hazards for the unwarly and unadvised business. Companies should speak with experienced counsel at an early stage to navigate through regulatory obstacles, and eliminate headaches and significant costs at a later time.

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