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## Private Offering: An Effective Capital Raising Method for Community Banks

**Legal Update**

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### What is a Private Offering?

Community banks require a consistent flow of incoming capital for growth and success in the market. One flexible and effective method bank holding companies can use to raise capital is a stock or capital notes offering (a “securities” offering). Typically, these offerings are structured as private offerings to a select number of investors. Private offerings must be conducted in strict accordance with a number of federal and state banking and securities laws, but for most community banks, they are a better, cheaper, and quicker way to raise capital than through a public offering.

### Why Conduct an Offering Now?

Not only is a securities offering an effective way for a community bank to raise capital, but also now might be the right time to conduct a private offering. According to a CNBC survey released in April, more than 80 percent of professional investors believe U.S. publicly traded stocks are overpriced. Accounting for these high prices and volatility of the stock market, investors have increasingly been taking advantage of alternative investment strategies beyond purchasing publicly traded stock and bonds. In particular, investors are currently seeking out privately-held companies, such as community banks, to achieve above average returns.

### Process for Conducting a Private Offering

The process for conducting a private offering generally includes three main steps: 1) pre-offering organization, 2) creation of required documents, and 3) marketing to new investors. Each step is crucial to properly conduct a private offering.

Pre-offering organization includes tasks such as determining the amount of shares or notes to be sold, the price, the minimum investment allowed for each investor, how the transaction will be structured overall, and whether any of the company’s governance documents or agreements (such as a shareholder or “buy-sell” agreement) will restrict the company’s ability to conduct the private offering. This

step is also where a bank holding company seeking to administer a private offering must choose the SEC exemption that best fits under Regulation D of the Securities Act of 1933. A well-structured transaction is also important in communicating professionalism to potential investors.

After the transaction has been structured, a company seeking to conduct a private offering must create a set of required documents. The primary required document is an offering memorandum that includes important representations about the company, its bank, the transaction structure, and any risks that should be communicated to investors. Another required document is a subscription agreement which the investors enter into when purchasing the securities. Registration with the SEC is done by filing a "Form D," which requires basic information about the company and the offering, and must be filed with the SEC within 15 days of the first sale. Companies conducting a private offering also need to comply with any state securities laws.

The final step is to market the securities to investors. Current shareholders and directors are an obvious place to start. If a more general solicitation is desired, the company can approach others in the community or spread the net even wider and offer the securities in a general solicitation. In many cases, purchasers must be accredited investors. Accredited investors are generally high net worth individuals and large institutional investors such as investment banks and pension funds. Ultimately, the marketing strategies permitted for any given private offering depend upon the SEC exemption chosen for the offering under Regulation D of the Securities Act.

## Takeaway

A private securities offering is an excellent way to raise capital, but be careful to make sure your offering complies with regulatory requirements (including those discussed in this article) as well as any requirements in your governance documents or agreements.