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SEC proposes amendments to Rule 701 and Form S-8 to respond to the evolution of the "gig economy" and to modernize Rule 701 and Form S-8

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The Securities and Exchange Commission has proposed rule changes that, on a temporary basis and subject to limits and conditions, would permit an issuer to provide equity compensation to "platform workers" who provide services available through the issuer's technology-based platform or system. The proposed rules would amend Rule 701, which provides a mechanism for non-public companies to issue equity-based compensation, and Form S-8, which is a registration statement used by public companies to issue equity-based compensation to employees and consultants. The proposed rules are intended to update SEC rules relating to equity compensation in order to better take into account the development of the "gig economy" and related changes in the composition and participation of today's workforce. These amendments, if adopted, could assist developing non-public companies in attracting talented platform workers to assist them in implementing growth plans by increasing the availability of equity incentive compensation to augment cash compensation demands on non-public and reporting companies that access platform workers in today's gig economy.

The proposed rule changes were made to address comments received from the public on a July 2018 SEC concept release that requested suggestions for updates to Rule 701 and Form S-8. The comment release was issued in response to a legislative mandate under the Economic Growth, Regulatory Relief and Consumer Protection Act.

In addition to the proposed amendments relating to platform workers, the SEC has proposed amendments to Rule 701 and Form S-8 to update them to reflect changes in practices and regulation since the adoption of the last updating amendments of Rule 701 and Form S-8.

Proposed amendments to account for the development of the gig economy

In recognition of changes to the ways in which companies receive services from employees and others and the development of the gig economy in which companies receive services from both permanent employees and freelancers, the SEC has proposed amendments, on a trial basis, to permit non-public companies to use an expanded registration exemption under Rule 701 to issue securities to an expanded group of service providers, to be called "platform workers," and to include

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the offer and sale of securities by a public company to that expanded group of service providers in a registration under Form S-8.

Proposed expansion of Rule 701 for issuances to platform workers. The SEC has proposed to amend Rule 701, on a trial basis for a temporary period of five years, to permit non-public companies to issue, subject to certain conditions, securities as compensation to platform workers who, pursuant to a written plan or agreement, provide services via a computer-based platform or other widespread, technology-based marketplace or system. The term "platform workers," as proposed by the SEC, would consist of workers, which may be either individuals or entities, unaffiliated with the issuer who provide bona fide services to the issuer, its parents or subsidiaries, or to third parties where such services benefit the issuer, via the company's internet-based or other widespread marketplace or system and pursuant to a written plan or agreement.

The proposed conditions to the exemption are:

— the issuer must operate and control the platform as demonstrated by the issuer's ability to provide access to the platform, to establish the principal terms for using the platform, and terms and conditions by which platform workers receive compensation for performing services and to accept and remove platform workers participating on the platform;
— the issuance of securities to platform workers must be made pursuant to a compensatory arrangement evidenced by a written compensation or contract, and not for services relating to capital-raising securities transactions or the promotion or maintenance of a market for the issuer's securities;
— no more than 15% of the value of compensation received by a participating worker from the issuer for services provided by means of the platform during a 12-month period and no more than $75,000 of such compensation received by the worker during a 36-month period may consist of securities based on their value at the time of grant;
— the amount and terms of securities issued to a platform worker must not be subject to individual bargaining or the worker's ability to elect between payment in securities or cash; and
— the issuer must take reasonable steps to impose transfer restrictions on the securities issued pursuant to the exemption other than sales back to the issuer or by operation of law.

Proposed amendments to Form S-8 for platform workers. The SEC proposal would amend Form S-8 to permit a company that reports pursuant to the Securities Exchange Act of 1934 to register the offer and sale of securities to platform workers on Form S-8 subject to the same conditions that apply to eligibility for the expanded exemption under Rule 701. The amendments, if adopted, also would apply on a five-year temporary basis.

Reporting obligations. In order to assist the SEC in assessing the Rule 701 and Form S-8 amendments during the five-year trial period, companies issuing securities to platform workers would be subject to an obligation to report at six-month intervals information regarding such issuances.

Proposed amendments to update Rule 701 and Form S-8

Proposed Rule 701 updates. The principal proposed modernizing amendments to Rule 701 would:

- revise financial disclosure requirements applicable to Rule 701 exempt transactions exceeding $10 million;
- revise the time at which disclosure under Rule 701 is required for derivative securities that do not involve a decision by the holder to exercise or convert in specified circumstances where derivative securities are issued to new hires;
- raise caps on the amount of securities that non-public companies may sell under Rule 701 during any 12-month period; and
- permit the Rule 701 exemption to be available for securities issuances pursuant to a written compensatory benefit plan or written compensatory contract established by subsidiaries, whether or not majority-owned, of non-public companies.

Proposed Form S-8 updates. The principal proposed clarifying and modernizing amendments to Form S-8 would:

- permit companies to add multiple plans to a single Form S-8;
- permit companies to securities or classes of securities to a Form S-8 with automatic effectiveness;
- eliminate the requirement to disclose the tax effects of plan participation; and
- enhance share counting and fee payments under the Form and conform Form S-8 instructions to Internal Revenue Service plan review practices.

Proposed updates to both Rule 701 and Form S-8. The SEC also proposed to amend both Rule 701 and Form S-8 to:

- extend the eligibility of consultants and advisors to entities meeting specified ownership criteria that link the securities to the performance of services; and
- extend eligibility of former employees to specified post-termination grants and former employees of acquired entities.

The comment period for these proposals will remain open until February 9, 2021.

For more information on the content of this alert, please contact your Nixon Peabody attorney or:

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