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Davis Polk

Davis Polk & Wardwell LLP
450 Lexington Avenue
New York, NY 10017

212 450 4000 tel
212 701 5800 fax

Re: Comments on Compensatory Securities Offerings and Sales; File Number S7-18-18

September 24, 2018

VIA E-MAIL: rule-comments@sec.gov

Mr. Brent J. Fields
Secretary
Securities and Exchange Commission
100 F Street NE
Washington, DC 20549-1090

Dear Mr. Fields:

We are submitting this letter in response to the solicitation by the Securities and Exchange Commission (the "**Commission**") for comments on the Rule 701 exemption from registration under the Securities Act of 1933, as amended (the "**Securities Act**") for securities issued by non-reporting companies pursuant to compensatory arrangements; and Form S-8, the simplified registration statement for compensatory offerings by reporting companies. On July 18, 2018, the Commission issued a concept release (the "**Concept Release**") that was published in the Federal Register on July 24, 2018 to solicit comments on (i) ways to modernize the regulatory regime for compensatory securities offerings and sales to address recent developments such as changes to equity compensation, and the rise of "gig economy" alternative work arrangements; (ii) whether the Commission should further revise the disclosure content and timing requirements of Rule 701(e); and (iii) whether the use of Form S-8 should be further streamlined. [1]

We appreciate the Commission's interest in reducing the burden of compliance and providing flexibility to companies by updating the eligibility, disclosure and timing requirements of Rule 701 and considering further streamlining of Form S-8. In response to the questions posed by the Commission, we respectfully request that the Commission consider the following recommendations for changes to Rule 701 and Form S-8.

Rule 701(c) Eligible Plan Participants

To what extent should definitions of "employee" under other regulatory regimes guide our thinking on eligible participants in compensatory securities offerings? Which regulatory regimes should we consider for this purpose? Should any new test apply equally to all companies, or would there be a reason to apply different tests based on the nature of the working relationship? (Question 1)

Would the application of Rule 701 to consultants and advisors in any circumstances cover the alternative work arrangements described above? (Question 2)

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[1] Concept Release on Compensatory Securities Offerings and Sales, Release No. 33-10521 (Jul. 18, 2018) [83 FR 34958 (July 24, 2018)].

What, if any, services should an individual participating in the "gig economy" need to provide to the issuer to be eligible under Rule 701? Do these individuals in fact provide services to the issuer, or instead to the issuer's customers or end users? Should this fact make any difference for purposes of Rule 701 eligibility? (Question 3)

Should we consider a test that identifies Rule 701 eligible participants as individuals who use the issuer's platform to secure work providing lawful services to end users? (Question 4)

Are any other factors necessary to establish any level of control by the issuer, such as requiring the work to be assigned by the issuer? Or is it necessary that the issuer control what the individual charges end users for services, such as by setting hourly rates or ride fares? Should a written contractual relationship between the issuer and individual be necessary? Why or why not? (Question 4(a))

Does it matter whether the issuer controls when and how the individual receives monetary compensation for the services provided? (Question 4(c))

We support extending eligibility for the Rule 701 exemption to offers and sales to service providers of all forms, including gig economy workers as well as corporate entities that provide services, including personal services businesses. We agree, as the Commission noted in the Concept Release, that gig economy workers may not necessarily be "employees", "consultants", "advisors" or "de facto employees" who are currently eligible to receive securities in compensatory arrangements under Rule 701.[2] As discussed later in this letter, we recommend conforming Form S-8 eligibility to any expansion of Rule 701 eligibility.

Gig Economy Relationships Should Be Treated as a New and Distinct Category for Purposes of Rule 701.

In order to avoid eroding the established scopes of the current categories of persons eligible to receive securities under Rule 701, we believe that gig economy alternative work arrangements should be treated for purposes of Rule 701 as a new and distinct category of relationship between issuers and workers. This relationship may, in certain cases, include services that constitute or resemble service as an employee, consultant or advisor, but would also encompass services outside the scope of those categories, including services to or transactions with the end users of an issuer's platform. We believe that neither particular definitions of employee nor the concept of employment generally should constrain the availability of Rule 701 to gig economy workers. If anything, recent and ongoing developments suggest that, while the employment relationship remains predominant, service relationships are evolving in ways that have shifted large numbers of service providers into alternative work arrangements that do not necessarily involve a classic employer-employee relationship.[3]

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[2] Concept Release at Section II.B.

[3] *See, e.g., Freelancing in America 2017*, UPWORK (Oct. 17, 2017), https://www.upwork.com/i/freelancing-in-america/2017/ (finding 36 percent of U.S. workforce was freelancing in 2017 and annually contributing approximately $1.4 trillion to the economy; and predicting 50 percent of U.S. workforce would be freelancers by 2027); Emilia Istrate & Jonathan Harris, National Association of Counties, *The Future of Work: The Rise of the Gig Economy* (Nov. 2017), available at http://www.naco.org/featured-resources/future-work-rise-gig-economy (citing 19 percent growth in the number of self-employed workers (many of whom were gig economy workers) and the nearly 21 percent growth in such workers' gross receipts, between 2005 and 2015); McKinsey Global Institute, *Independent work: Choice, necessity and the gig economy* (Oct. 2016), available at https://www.mckinsey.com/~/media/McKinsey/Featured%20Insights/Employment%20and%20Growth/Independent%20work%20Choice%20necessity%20and%20the%20gig%20economy/Independent-Work-Choice-necessity-and-the-gig-economy-Full-report.ashx (observing rapid evolution of independent (i.e., gig economy) work due to evolution of digital platforms, worker interest in becoming independent, large population of people who want to work and increased demand for independent services; citing benefits of independent work, including lower unemployment, higher demand, productivity and availability of services and more autonomy and flexibility for workers); Abdullahi Muhammed, *4 Reasons Why The Gig Economy Will Only Keep Growing in Numbers*, FORBES (Jun. 28, 2018), https://www.forbes.com/sites/abdullahimuhammed/2018/06/28/4-reasons-why-the-gig-economy-will-only-keep-growing-in-numbers/#4b5305c411eb (citing gap between supply and demand for educated workers, changing attitudes towards

Gig Economy Workers Should Not Have to Satisfy Minimal Level of Income Relationship with an Issuer to Be Eligible to Participate in a Rule 701 Offer or Sale of Securities.

In connection with evaluating whether and how gig economy workers should be eligible to participate in a Rule 701 offer or sale of securities, we would expect that many gig economy workers would not satisfy the "primary source of earned income" requirements for treatment as "de facto employees"[4] for purposes of Rule 701 eligibility. As the Commission noted in the Concept Release,[5] gig economy workers commonly provide goods or services through multiple issuer platforms, and thus may not receive 50 percent or more of their income from a single issuer.[6] Accordingly, we respectfully suggest that gig economy workers should not need to satisfy any minimal level of income relationship with an issuer in order to be eligible to participate in an issuer's offers or sales of securities exempted under Rule 701.

Gig Economy Workers Need Not Be Natural Persons to Be Eligible to Participate in Rule 701 Offerings.

We further suggest that gig economy workers need not be natural persons to be eligible to participate in a Rule 701 offering or sale. Gig economy workers may provide services to issuers either directly or indirectly through personal services businesses, "the principal activity of which is the performance of personal services and such services are substantially performed by employee-owners".[7] Although the Commission's general policy has been to favor grants to natural persons,[8] the Commission has recognized personal services businesses as "alter egos" of the natural persons with respect to their eligibility to participate in Form S-8 offerings as employees[9] and as consultants or advisors, stating that "in the limited circumstance where a consultant or advisor performs services for the issuer through a wholly owned corporate alter ego, we will continue to permit issuers to register on Form S-8 securities issued as compensation to that

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(continued...) work, employer cost-cutting and project-based hiring and changes in technology and infrastructure as factors contributing to growth of gig economy).

[4] *See* Rule 701—Exempt Offerings Pursuant to Compensatory Arrangements, Release No. 33-7645 (Feb. 25, 1999) [64 FR 11095 (Mar. 8, 1999)] [hereinafter "1999 Adopting Release"] at Section II.D ("a person in a de facto employment relationship with the issuer, such as a non-employee providing services that traditionally are performed by an employee, with compensation paid for those services being the primary source of the person's earned income, would qualify as an eligible person under the exemption"); *see also* Foundation Health Corporation, SEC No-Action Letter (July 12, 1993) (issuer permitted to use Form S-8 to register options granted to physicians who derived at least 50 percent of their earned income from services provided indirectly to issuer); LPL Holdings, Inc. and Linsco/Private Ledger Corp. SEC No-Action Letter (Apr. 18, 2001) (Commission staff found independent contracted sales and service agents who expected to derive majority of earned income from services provided to issuer to be "de facto" employees eligible to receive compensatory grants made in reliance on Rule 701); SEC Department of Corporation Finance Compliance and Disclosure Interpretation [hereinafter "C&DI"] 226.02 Securities Act Forms (Feb. 27, 2009), available at https://www.sec.gov/divisions/corpfin/guidance/safinterp.htm (issuer denied use of Form S-8 to cover issuance of options to independent pharmaceutical distributors that issuer considered to be de facto employees, because Commission staff found "the nature of the services provided to the issuer would be Amway-style pyramid 'network distribution', which would not necessarily be income, the primary source of the distributors' earned income").

[5] Concept Release at Section II.B.

[6] *See, e.g.,* Miranda Katz, *This App Lets Drivers Juggle Competing Uber and Lyft Rides*, WIRED (Feb. 15, 2018), https://www.wired.com/story/this-app-lets-drivers-juggle-competing-uber-and-lyft-rides (("Nearly 70 percent of on-demand drivers work for both Uber and Lyft, and one-quarter drive for more than just those two, according to a survey by The Rideshare Guy, a popular website for rideshare drivers.").

[7] 26 U.S.C. § 269A(b)(1).

[8] *See* Image Entertainment, SEC No-Action Letter (Mar. 6, 1992) (Commission denied the use of Form S-8 to cover an option grant made to U.S. Connections, Inc. as consultant or advisor to Image Entertainment. Kasper argued that U.S. Connections, Inc., which was a personal services corporation of which Kasper was the sole shareholder and employee, was his alter ego.

[9] *See* Aaron Spelling Productions, SEC No-Action Letter (July 1, 1987) (issuer allowed use of Form S-8 to cover a company's compensatory grant to individuals paid through a personal services corporation because "except that their compensation is technically paid to a corporation, such individuals are indistinguishable from other employees with regard to either services provided to, or knowledge of, the Company").

corporate entity".[10] This treatment of personal services businesses with respect to Form S-8 seems applicable to Rule 701 as well, in light of how the Commission quickly harmonized the interpretation of consultants and advisors in Rule 701 to match the narrower interpretation in Form S-8.[11] We respectfully suggest that this treatment be extended to gig economy workers, so that such workers are eligible for equity awards exempt under Rule 701, regardless of whether their alternative work arrangement involves a personal services business.

Corporate Entities That Are Providing Services to an Issuer or Other Qualified Entities Should Be Eligible to Participate in Rule 701 Offers and Sales.

Furthermore, in conjunction with, and in addition to, extending Rule 701 to cover gig economy workers, we recommend that the Commission expand the characterization of corporate alter egos eligible to receive compensatory grants made under Rule 701 to cover entities wholly owned by multiple natural person services providers or by the management of the entities. There is no policy rationale for the current requirement that for entities to be eligible to receive compensatory grants made by an issuer under Rule 701, such entities must be wholly owned by (or jointly owned with spouses of) natural persons providing services to the issuer.[12]

Gig Economy Workers and Corporate Service Providers Should Not Be Eligible to Participate in Rule 701 Offers and Sales if Involved in Capital Raising for the Issuer.

We also believe that with respect to extending Rule 701 eligibility to gig economy workers and corporate service providers, no persons involved in capital raising for the issuer should be eligible to participate in an issuer's offers and sales of securities pursuant to compensatory plans or contracts. The Commission has historically been concerned about the potential abuse of Rule 701 and Form S-8 to cover grants to consultants and advisors purportedly made for compensatory purposes, but actually made for capital-raising purposes.[13] Maintaining the prohibition on the use of Rule 701 for capital raising would protect the intended purpose of the Rule 701 exemption, the facilitation of stock ownership among service providers of the issuer to align such service providers' economic interests with those of the issuer.

The Commission Should Not Consider Gig Economy Workers Who Receive Compensatory Grants Under Rule 701(c) to Be "Holders of Record" for the Purposes of Rule 12g5-1 under the Exchange Act.

Lastly, we recommend that the Commission not consider gig economy workers who receive compensatory grants under Rule 701 to be "holders of record" as defined in Section 12g5-1 of the Securities Exchange Act of 1934, as amended (the "**Exchange Act**").[14] Rule 12g5-1(b)(1) under the Exchange Act ("**Rule 12g5-1**") requires issuers to register a class of equity if they have 2,000 holders of record or 500 non-accredited investor holders of record.[15] Given that major gig economy issuers can have relationships with workers whose numbers greatly exceed these limits,[16] the extension of the Rule 701 offering exemption to gig

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[10] Registration of Securities on Form S-8, Release No. 33-7646 (Feb. 25, 1999) [64 FR 11103 (Mar. 8, 1999)] [hereinafter "1999 S-8 Adopting Release"], at note 29.

[11] 1999 Adopting Release at Section II.D.

[12] *See supra* note 8.

[13] *See* 1999 S-8 Adopting Release at Section I.A. (discussing issuer registration on Form S-8 of securities nominally offered to "so-called 'consultants'" who in some cases perform limited or no additional services to the issuers, and resell securities in the public markets as directed by the issuer or a promoter to apply the proceeds as remittances to the issuer or to pay expenses of the issuer unrelated to services provided by the consultants); 1999 Adopting Release at Section II.D (indicating concern that issuers would abuse Rule 701 for capital-raising purposes in the same manner as for Form S-8).

[14] 15 U.S.C. 78l(g)(1).

[15] 17 CFR 240.12g-1(b)(1).

[16] *See, e.g.,* ETSY, *Etsy, Inc. Reports Second Quarter 2018 Financial Results* (Aug. 6, 2018), available at https://investors.etsy.com/news-and-events/press-releases/2018/08-06-2018-210856618 (stating Etsy has close to 2 million active sellers).

economy workers would not be meaningful if such workers are considered holders of record for purposes of Rule 12g5-1. We suggest that gig economy workers should fall under the Section 12(g)(5) safe harbor implemented by Section 502 of the Jumpstart Our Business Startups Act[17], which allows issuers to exclude individuals who received equity pursuant to Rule 701(c) from being considered holders of record for purposes of determining whether an issuer is required to register a class of equity.[18]

Rule 701(e) Disclosure Requirements: Timing and Manner of Rule 701(e) Disclosure

Should we consider other alternatives to the Regulation A financial statements currently required for reliance on Rule 701, such as short-form rather than long-form financial statements? (Question 29)

The Commission Should Allow Issuers to Provide Short-Form, Instead of Long-Form, Financial Statements for Purposes of Rule 701.

We recommend that the Commission consider other alternatives to the Regulation A financial statements currently required for reliance on Rule 701 in the event that the now $10 million threshold is exceeded. Issuers currently relying on Rule 701 may choose to comply with the financial statements requirements of either Tier 1 or Tier 2 companies as prescribed in Part F/S of Form 1-A,[19] but must provide as a baseline two years of consolidated balance sheets, statements of income, cash flows and changes in stockholders' equity.[20] Such financial statements must be as of a date no more than 180 days before the date of sale.

As the Commission noted in the Concept Release,[21] these requirements mean that, in order to engage in continuous sales of equity, issuers must make their financial statements available on at least a quarterly basis, and complete them within three months after the end of each quarter. This is a significant administrative burden for issuers. We believe that allowing issuers to provide short-form, instead of long-form, financial statements for the purposes of Rule 701 would reduce this burden, and encourage more issuers to make compensatory grants. We also believe that short-form financial statements would provide grant recipients with sufficient disclosure, given that "the issuer is concerned primarily with compensating the employee-investor rather than maximizing its proceeds from the sale",[22] and because such recipients have access to issuer financial statements furnished in connection with other filings.

Because foreign private issuers that are subject to the Exchange Act reporting requirements generally are not required to submit quarterly financial statements, should non-reporting foreign private issuers that rely on Rule 701 be subject to the condition to provide quarterly financial statements if they continue to sell securities throughout the year? (Question 31)

Foreign Private Issuers Should Be Allowed to Sell Securities Throughout the Year Under Compensatory Plans in Reliance on Rule 701 as Long as They Produce Financial Statements as Frequently as Required of Them Under the Law of Their Home Jurisdiction.

We believe that non-reporting foreign private issuers should be allowed to sell securities throughout the year under compensatory plans in reliance on Rule 701 as long as they produce financial statements as frequently as required of them under the law of their home jurisdiction.

Rule 701(e)(4)[23] requires issuers who have exceeded the $10 million threshold to provide financial statements that must be as of a date no more than 180 days before the date of any sale in reliance on Rule

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[17] Sec. 502, 126 Stat. at 326.

[18] 15 U.S.C. 78l(g)(5).

[19] Regulation A Offering Statement [17 CFR 239.90].

[20] 17 CFR 210.1-01 through 201.12-29. *See* Part F/S of Regulation A Offering Statement [17 CFR 239.90].

[21] Concept Release at Section II.C.1.

[22] 1999 Adopting Release at Section II.B.

[23] 17 CFR 230.701(e)(4).

701. As the Commission acknowledged in the Concept Release,[24] this means that an issuer seeking to maintain current information must make financial statements available on at least a quarterly basis or place a moratorium on Rule 701 offerings. This requirement places an unnecessary burden on foreign private issuers ("**FPIs**") that are not registered in the United States, and are not required to submit quarterly financial statements in their home jurisdictions. For example, the home country regulators of FPIs listed on stock exchanges in the United Kingdom, France,[25] Switzerland[26] and Hong Kong[27] require semi-annual, rather than quarterly, financials, and FPIs have complied accordingly.[28] Furthermore, issuers that use the International Financial Reporting Standard typically do not prepare full balance sheets, income statements and cash flow statements on a quarterly basis.[29]

FPIs that are registered in the United States can make use of Form S-8 to make broad offers of securities under compensation plans without providing financial statements more frequently than required by home country regulators. As a result, FPIs that rely on Rule 701 are currently subject to a more stringent financial reporting scheme in the United States than U.S.-registered FPIs that offer securities registered under Form S-8. In addition, U.S. recipients of FPIs that are not registered in the United States and make compensatory grants relying on Rule 701 are at a disadvantage to employees of U.S.-registered FPIs that make grants of securities registered under Form S-8 if they receive stock options or other derivative securities. Given that Rule 701(e)(6)[30] requires issuers to deliver disclosures "a reasonable time" before exercise or conversion of such derivative securities, employees of FPIs that are not registered in the United States may be subject to a period of time in which they cannot exercise stock options issued by their employer.

We believe that with regard to FPIs, it should not be necessary to impose a more stringent standard on non-U.S. reporting companies than on U.S. reporting companies. We therefore recommend that Rule 701 be amended to allow FPIs to satisfy the requirements of Rule 701(e)(4) if they comply with the exemption under Rule 12g3-2(b)(1),[31] and timely post in English on their website all periodic financial reports that their home country regulators require them to publish.[32]

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[24] *See supra* note 21.

[25] The United Kingdom and France removed the quarterly requirement in response to Directive 2013/50/EU of the European Parliament and of the Council of 22 October 2013 amending Directive 2004/109/EC of the European Parliament and of the Council on the harmonisation of transparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market, Directive 2003/71/EC of the European Parliament and of the Council on the prospectus to be published when securities are offered to the public or admitted to trading and Commission Directive 2007/14/EC laying down detailed rules for the implementation of certain provisions of Directive 2004/109/EC Text with EEA relevance, 2013 OJ L 294.

[26] Bundesgesetz vom 30. März 1911 betreffend die Ergänzung des Schweizerischen Zivilgesetzbuches (Fünfter Teil: Obligationenrecht), AS 2017, Art. 958 Obligationenrecht Ans. 3.

[27] THE STOCK EXCHANGE OF HONG KONG LIMITED, *Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited*, Section 13.48(1) (last accessed Sept. 22, 2018), available at http://en-rules.hkex.com.hk/en/display/display_main.html?rbid=4476&element_id=1932.

[28] *See, e.g.,* Owen Walker, *The long and short of the quarterly reports controversy*, FINANCIAL TIMES (July 1, 2018), https://www.ft.com/content/e61046bc-7a2e-11e8-8e67-1e1a0846c475 (finding that between October 2016 and August 2017, the number of companies issuing quarterly reports fell from 70 to 57 among FTSE 100 companies and from 111 to 83 among FTSE 250 companies).

[29] *See* International Accounting Standard 34 - Interim Financial Reporting (recommending that public companies "provide interim financial reports at least as of the end of the first half of their financial year").

[30] 17 CFR 230.701(d)(iv)(6).

[31] 17 CFR 240.12g3-2(b)(1).

[32] 17 CFR 240.12g3-2(b)(2).

Rule 701(e) Disclosure Requirements: Options and Other Derivative Securities/RSUs

Should Rule 701 be amended to specifically address when disclosure is required for RSUs? If so, when should Rule 701(e) disclosure be required for an RSU? Should we revisit the concept of "convert or exercise" as providing the relevant date for disclosure? For new hires who receive RSUs, should we require that disclosure be provided within 30 days after commencing employment? If not, when should Rule 701(e) disclosure be required for RSUs issued to new hires? (Question 37)

The Commission Should Amend Rule 701 to Provide for Reliance on Rule 701 if There Is a Legitimate Reason to Delay Information Delivery to After the Date of Grant of an RSU Award.

RSU awards do not involve any direct cost to the recipient, and accordingly should be generally covered by the "no-sale" theory for registration exemption, as acknowledged by the Commission with respect to similar awards made available to a relatively broad group of employees.[33]. The Commission takes the position that the date of sale for a restricted stock unit ("RSU") award in reliance on Rule 701 is the date the award is granted,[34] and thus an issuer that has exceeded the $10 million threshold must provide information pursuant to Rule 701(e) "a reasonable time before the date" the RSU is granted.[35] This position is based on the Commission's views that (i) RSUs are not "exercised or converted" within the meaning of Rule 701(e)(6) and (ii) instruments such as RSUs settle by their terms without the recipient taking an action to exercise or convert.

While we agree that the recipient of an RSU need not take any specific act to exercise and convert an RSU award, and that the date of grant stands out as the date on which the recipient is most likely to make something like an investment decision with respect to the award, we also recognize that an RSU award recipient must provide service for what is generally an extended period of one to three or more years in order to earn the award. As such, the recipient could be seen to have made some fraction of his or her investment decision with respect to a then unvested award on each day he or she continues to work for the issuer during the vesting period. While this view does not point to any clear time other than the grant date or vesting date in which the total investment decision with respect to an RSU award is made, it does suggest that there could be room for flexibility in establishing when information must be provided in order to be timely with regard to the recipient's ongoing investment decision. Accordingly, we believe that, where there is a legitimate reason to delay the delivery of information to a time after the date of grant of an RSU award, it would be reasonable for the Commission to amend Rule 701 to provide that such a delay would not prevent the award from relying upon Rule 701.

Are there any other instruments that should be specifically addressed in the rule? (Question 39)

Rule 701 Should Specifically Address the Valuation of Profits Interests for Purposes of the Rule.

We recommend that Rule 701 specifically address the valuation of profits interests for purposes of the rule. We support the current Internal Revenue Service (the "**IRS**") approach to the valuation of profits interests under IRS Revenue Procedures 93-27 and 2001-43[36] — that the receipt of a qualifying profits interest is not a taxable event, and, for purposes of the determination of whether an interest granted to a service provider is a qualifying profits interest, the interest is treated as received by the service provider on the date of grant, even if substantially unvested at that time. We believe, however, there is a need for clarity with regard to the implications of the grant date zero-value for purposes of Rule 701(e).

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[33] *See* Employee Benefit Plans; Interpretations of Statute, Release No. 33-6188 (Feb. 1, 1980) [45 FR 8960 (Feb. 11, 1980)] [hereinafter "Employee Benefit Plans Release"] at Section II.A.5.d; Employee Benefit Plans, Release No. 33-6281 (Jan. 15, 1981) [46 FR 8446 (Jan. 27, 1981)] at Section III.

[34] *See* SEC Department of Corporation Finance C&DI 271.24 Securities Act Rules (Nov. 6, 2017), available at https://www.sec.gov/divisions/corpfin/guidance/securitiesactrules-interps.htm.

[35] *See* 17 CFR 230.701(e).

[36] Rev. Proc. 93-27, 1993-2 C.B. 343; Rev. Proc. 2001-43, 2001-2 C.B. 191.

We recognize that not all profits interests are afforded zero-value treatment under IRS Rev. Proc. 93-27, which does not purport to address profits interests that (i) are not received in a partner capacity or in anticipation of being a partner, (ii) relate to a substantially certain and predictable stream of income from partnership assets, (iii) are disposed of by the recipient within two years of receipt or (iv) represent a limited partnership interest in a publicly traded partnership. That being said, in our experience, most pass-through entities issuing profits interests structure them with the intent to comply with IRS requirements for zero-value grant date treatment. Thus a pass-through entity's profits interests, if measured using the IRS method as of the date of grant, would not contribute any value to the aggregate sales price or amount of securities sold in any period for purposes of Rule 701(e).

In our view, the Commission could reasonably determine to apply the IRS' approach with regard to grant-date valuation of profits interests, and treat qualifying profits interests as having zero value for purposes of Rule 701. This approach would have the effect of exempting such offerings from the additional information requirements of 701(e), but this result does not offend our sensibilities given that the recipient is not required to provide any payment beyond their services to acquire the interest, and profits in many circumstances are entirely uncertain. The effect would be similar to the application of the "no-sale" theory for registration exemption, which should be available for qualifying profits interests in any case where the acquisition of the interest is not voluntary, such that the recipient did not make an investment decision.[37]

Form S-8: Form S-8 Eligible Plan Participants

To the extent we change the application of Rule 701 by changing the scope of individuals eligible for compensatory offerings, such as to include individuals participating in the "gig economy," should we make corresponding changes to Form S-8? Why or why not? If the scope of individuals who are eligible for Form S-8 offerings were expanded, would there be concerns about misuse of the form for capital raising activities? If so, how could we safeguard against those concerns? (Question 42)

To the Extent that the Commission Changes the Scope of Individuals Eligible for Compensatory Offerings Pursuant to Rule 701, it Should Make Corresponding Changes to Form S-8.

We recommend that to the extent that the Commission changes the scope of individuals eligible for compensatory offerings pursuant to Rule 701, it make corresponding changes to Form S-8. As discussed above with respect to expanding Rule 701 to include gig economy workers, the Commission previously harmonized its interpretation of consultants and advisors in Rule 701 and Form S-8 to circumvent abuses of the Rule 701 exemption in response to the Commission's limitation of consultant and advisor eligibility with respect to Form S-8.[38] A corresponding change to the scope of eligibility for offers under Form S-8 would maintain the current harmonization of eligible recipients under these two approaches, and avoid confusion on the part of issuers. While such an expansion of scope of eligibility could give rise to theoretical concerns about the misuse of Form S-8 for capital raising activities, given that unlike securities offered pursuant to Rule 701, securities registered under Form S-8 would not be restricted, we believe that such concerns are unfounded. Unlike the purported "consultants" that the Commission has previously found engaging in abuses of Form S-8 by selling securities granted by the issuer to the secondary market and remitting the proceeds to the issuer or using them to pay expenses of the issuer unrelated to services provided by the "consultants", gig economy workers provide real goods and services through the issuer's platform.[39] We also note that if the Commission does not broaden the scope of eligibility for Form S-8 to match a broadened scope for Rule 701, issuers who wish to extend equity compensation to gig economy workers may choose to remain private companies. Not only would such issuers be able to make offerings and sales to a wider scope of recipients under Rule 701, they would also remain subject to less onerous disclosure requirements than those of reporting companies. Given the Commission's commitment to encouraging the ongoing development and expansion of the public market, we believe that this disincentive against companies going public should override any concerns about the potential abuse of Form S-8.

We also recommend that if the Commission expands the scope of Rule 701 to include entities wholly owned by two or more employees or by management, it does the same for the scope of Form S-8 in order to expand employee equity ownership among reporting companies.

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[37] *See supra* note 33.

[38] *See* 1999 Adopting Release at Section II.D.

[39] *See supra* note 6.

In the Context of a Corporate Acquisition, Former Employees of a Target Company Should Be Eligible to Participate in the Acquiring Company's Form S-8 Registration With Respect to Equity Awards Granted in the Acquisition.

In addition, we suggest that the Commission expand the scope of eligible participants with respect to Form S-8 to address the context of a corporate acquisition. Former employees of the target company in an acquisition should be able to participate in the acquiring company's Form S-8 registration with respect to equity awards granted in the acquisition, in exchange for awards issued by the target company while such former employees were still with the company.[40] Such an expansion of eligibility would facilitate the rollover of employee equity holdings by reducing the administrative burdens that currently exist. These burdens may include the need to cancel target company equity awards held by former employees. It may also include the need to separately register awards, on a registration form other than Form S-8, of the acquiring company's stock issued to replace the target equity awards of former employees of the target company. These burdens do not provide any significant offsetting benefit to the former employees of the target company, who may prefer to retain their equity awards through the acquisition and would be informed of their rights with respect to the plan by a registration on Form S-8 as well as by a registration on any other form.

Form S-8: Administrative Burdens

Simplification of Form S-8 Registration of Sales under 401(k) Plans.

Should we further simplify the registration requirements of Form S-8? For example, does registering a specific number of shares result in Section 5 compliance problems when plan sales exceed the number of shares registered, such as for Section 401(k) plans and similar defined contribution retirement savings plans? If so, how should we address this issue? (Question 45)

We have found that the current provisions for registering shares offered under Section 401(k)[41] plans and similar defined contribution plans on Form S-8 can require substantial effort and expense on the part of plan administrators and record keepers in order to maintain compliance. The consequences of any failure in this respect can have a significant adverse impact on people or organizations operating in good faith, with the only clear remedy being offers of rescission to all affected plan participants. In part, the burden of administration arises from efforts to take conservative approaches to counting plan transactions against the available pool of registered shares. These efforts are due to a lack of clarity regarding how such transactions should be counted for this purpose, particularly exacerbated by the fact that plan participants hold interests in a stock fund, rather than individual securities, and make changes in investment funds on a dynamic basis before monetizing their balances.

The Commission Should Allow Registration of an Indefinite Number of Sales of Issuer Shares Under a 401(k) Plan.

In light of these concerns, we suggest that Form S-8 be revised to allow for registrations of offers or sales of employer securities under Section 401(k) plans and similar defined contribution retirement savings plans without requiring registration of a specific number of shares. In lieu of designating a specific number of shares, such plans should be allowed to register the sale of an indefinite number of shares, in the same way that such plans may now register the sale of an indefinite number of interests in the plan.

In order to satisfy the requirements of Section 6(c) of the Securities Act, Form S-8 could require any such plans seeking to register an indefinite number of shares to pay a filing fee based on the size of the issuer, measured by market capitalization at time of filing, or based on the issuer's filer status (e.g., accelerated filer, large accelerated filer, emerging growth company). Such a registration could be effective indefinitely or for a fixed period of time, such as five years, with the ability to extend by a simple post-effective amendment and payment of a further fee.

This approach would have the significant benefit of eliminating the need to track transactions in issuer shares under the plan in question, while otherwise maintaining the benefits of registration for plan shares.

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[40] *Cf.* SEC Department of Corporation Finance C&DI 126.14 Securities Act Forms (Feb. 27, 2009), available at https://www.sec.gov/divisions/corpfin/guidance/safinterp.htm.

[41] 26 U.S.C. 401(k).

Alternatively, the Commission Should Allow for the Correction of Sales in Excess of Registration by Retroactive Registration.

An alternative to the above approach would be to provide plans with a less burdensome means to correct sales in excess of the specific number of shares registered. One alternative would be to allow plans to retroactively register transactions in issuer shares under the plan by post-effective amendment or a follow-on Form S-8 and payment of an increased registration fee (e.g., an additional 15 to 20 percent fee) for good faith errors, with no time period limit for corrective filings to register additional securities, given that issuers may not detect deficiencies for a long time.

We believe that most issuers that provide for offers of issuer securities under their 401(k) and similar plans do so in whole or in part to benefit their employees. Further, under ERISA[42], plan administrators of 401(k) and similar plans are subject to fiduciary duties to act in the best interests of plan participants when evaluating whether the plans should offer employer securities as an investment alternative. As a result, we see little concern regarding abuse of 401(k) and similar plans as a means of offering issuer securities.

Use of a Single Form S-8 to Register Multiple Plans.

Should Form S-8 allow an issuer to register on a single form the offers and sales pursuant to all employee benefit plans that it sponsors? When shares are authorized for issuance by a given plan what information would need to be disclosed that would have been previously omitted from the effective registration statement? (Question 46)

The Commission Should Allow an Issuer to Register on a Single Form S-8 the Offers and Sales Pursuant to One or More of the Employee Benefit Plans That It Sponsors.

We believe that the Commission should allow an issuer to register on a single Form S-8 the offers and sales pursuant to one or more of the employee benefit plans that it sponsors. This approach could reduce the administrative burden of filing separate registration statements under Form S-8. To file a Form S-8, a company must prepare the form, collect the signatures from the requisite officers and at least a majority of current directors, obtain an opinion on the legality of shares and the consent of auditors whose reports are being incorporated by reference into the filing and pay a filing fee. Being able to register offers and sales pursuant to multiple employee benefit plans on a single Form S-8 would minimize the above requisite processes to the extent that plans are established or updated at the same time.

When shares are authorized for issuance by a given plan, the issuer could update the Form S-8 by post-effective amendment to include the name of the given plan and any increase in the number of shares authorized for issuance under such form. No further information should be required in the registration statement, but a separate prospectus addressing the information called for in Part I of Form S-8 should then be distributed with respect to that plan. For example, if an FPI has a compensatory plan with annual sub plans, the FPI could provide employees with a prospectus with regard to the material terms for each sub plan. The issuance system would resemble that of a shelf offering, which the Commission is accustomed to seeing in other securities offerings contexts.

If we facilitate a single registration statement for all employee benefit plan securities, should the number of shares to be registered continue to be specified in the initial registration statement? Alternatively, should issuers be able to add securities to the existing Form S-8 by an automatically effective post-effective amendment? If so, what would be the best way to implement such a system? (Question 47)

With respect to either alternative above, would the ability to have a single Form S-8 reduce administrative burdens given that many issuers currently monitor and track multiple registration statements on Form S-8? Would this be practicable where the securities to be registered relate to different forms of plans, such as Section 401(k) plans and incentive plans? Would it be practicable if some of the plans involved the issuance of plan interests, which trigger the individual plan's obligation to file an Exchange Act annual report on Form 11-K? Would the offer and sale of shares pursuant to multiple plans registered on the same Form S-8 create difficulties keeping track of which registered shares are being issued pursuant to which plan? (Question 48)

[42] The Employee Retirement Income Security Act of 1974 (29 U.S.C. 1001 et seq.).

We suggest that, if Form S-8 allows securities for more than one employee benefit plan to be registered on a single form, the form should allow the addition of shares by way of post-effective amendments. This would be necessary in order to allow the single form to cover securities offered under new plans established by the issuer, and new authorizations of shares under then existing plans.

While it might not be practicable for all issuers to include all of their equity plans in a single Form S-8, given the option, we believe that a substantial number of issuers would find some benefit from combining at least two or three of their plans in a single Form S-8, particularly when plans have similar characteristics and are approved or updated around the same time.

Payment of Registration Fees on a Periodic Basis.

[S]hould we require the payment of registration fees on a periodic basis with respect to the securities, the offer and sale of which were registered on Form S-8, during the prior period? How would such a system best be implemented? How could we structure such a system consistent with the requirements of Securities Act Section 6(c)? (Question 50)

A carry-forward filing fee payment system would reduce the administrative burden currently placed on issuers, who need to calculate reasonable estimates of offering sizes in advance. This can be difficult when issuers are hiring many employees and granting equity to such employees in a short period of time, or when unforeseen changes in senior management occur, requiring issuers to make large sign-on grants.

Other Ways to Reduce Administrative Burdens.

Are there any other ways to reduce the administrative burdens associated with filing and updating Form S-8? (Question 51)

We have a number of suggestions on other ways to reduce the administrative burden associated with filing and updating Form S-8 as follows:

- Form S-8 should provide that the inclusion of recent reports provided by Item 3(b) of Part II of Form S-8[43] could be satisfied by including the statement that all such reports are incorporated by reference, without requiring the issuer to identify each such report separately. This would be consistent with the approach with regard to all reports filed after the Form S-8, and seems appropriate given the broad availability of all such reports on the Commission's EDGAR website.

- The Commission should eliminate the requirement pursuant to Item 8 of Part II of Form S-8[44] and Item 601(b)(5) of Regulation S-K[45] to include, for a Section 401(a)[46] qualified plan, either a determination letter from the IRS or, alternatively, an opinion of counsel that "confirms compliance of the provisions of the written documents constituting the plan with the requirements of ERISA pertaining to such provisions".[47] In 2016, the IRS modified its determination letter program, as described in IRS Revenue Procedure 2016-37,[48] and under the new program, a sponsor of a qualified plan may only apply for a determination letter under limited circumstances. As a result, sponsors of qualified plans no longer seek periodic determination letters from the IRS. Accordingly, requiring an issuer to provide a determination letter, or alternatively an opinion of counsel, is overly burdensome to issuers, and is unnecessary given that the IRS no longer deems it useful for plan sponsors to seek regular determination letters.

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[43] Item 3(b) of Part I of Form S-8.

[44] Item 8 of Part II of Form S-8.

[45] 17 CFR 229.601(b)(5) (Item 601(b)(5) of Regulation S-K).

[46] 26 U.S.C. § 401(a).

[47] 17 CFR 229.601(b)(5)(ii)(A) (Item 601(b)(5)(ii)(A) of Regulation S-K).

[48] Rev. Proc. 2016-37, 2016-29 I.R.B. 13.

- The Commission should clarify that the sponsor of an employee benefit plan whose interests are being registered can sign the Form S-8 on behalf of the plan. Currently the instructions require the plan trustee to sign the Form S-8.[49] Current widespread market practice is for trustees of qualified employee benefit plans to be directed trustees who do not make investment decisions on behalf of the plan. It is administratively burdensome and unnecessary for plan sponsors to have to seek a trustee signature for the purpose of filing a Form S-8.

- The Commission should reconsider the requirement under Item 1(f) of Form S-8[50] to describe the tax effect that may accrue as a result of participating in an employee benefit plan, and the tax effects, if any, upon the registrant. Tax effects depend on individual tax circumstances, which can vary greatly from one plan participant to another. This is particularly true in light of the new deduction for qualified business income under Section 199A[51] of the Internal Revenue Code of 1986, as amended, which could result in different tax considerations for consultants and advisors relative to employees. Moreover, if the Commission expands the eligibility scope of Form S-8 to gig economy workers, such an expansion could result in different tax consequences for such workers relative to consultants, advisors and employees of an issuer. Providing generalized tax effect disclosures may thus be more misleading than informative to plan participants.

- It would ease the burden of completing the form if all relevant guidance issued to date by the Commission or Commission Staff, including guidance from C&DIs,[52] were included directly in Form S-8 to the extent practicable.

Form S-8: Form S-8 Generally

It has been suggested that Form S-8 registration would no longer be necessary if the Commission were to extend the Rule 701 exemption to Exchange Act reporting companies. What would be the advantages and disadvantages of allowing Exchange Act reporting companies to use Rule 701 and, in turn, eliminating Form S-8? Would permitting Exchange Act reporting companies to use Rule 701 raise any investor protection concerns or be inconsistent with the purposes underlying Rule 701? (Question 53)

The Commission Should Extend the Rule 701 Registration Exemption to Reporting Companies so That Such Companies Can Choose Between Using the Rule 701 Exemption or Form S-8 Registration for Offers and Sales of Compensatory Equity.

We support the Commission extending the Rule 701 registration exemption to reporting companies so that such companies can choose between using the Rule 701 exemption or Form S-8 registration for offers and sales of compensatory equity. We believe that the Commission should not eliminate Form S-8 in turn upon allowing reporting companies to use the Rule 701, but keep Form S-8 available as an alternative to the use of Rule 701, given that each mode of compensatory offers and sales has specific advantages as discussed below.

Advantages of Offerings Under Form S-8.

As a registration statement under the Securities Act, Form S-8 provides compensatory benefit plan participants with protection against material misstatements or omissions. Section 11 of the Securities Act provides strict liability protection for any material misstatements or omissions in Form S-8 at the time of filing,[53] while Section 12(a)(2) of the Securities Act provides a basis for liability if the prospectus delivered in conjunction with the Form S-8 filing contains any material misstatements or omissions.[54] However, there

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[49] Instructions 1. for Signatures for Form S-8.

[50] 17 CFR §230.428(b)(1); Item 1(f) of Part I of Form S-8; General Instructions A.1.(a)(1) to Form S-8.

[51] 26 U.S.C. § 199A.

[52] *See, e.g.,* SEC Department of Corporation Finance C&DI 126.03 Securities Act Forms (Feb. 27, 2009), available at https://www.sec.gov/divisions/corpfin/guidance/safinterp.htm; SEC Department of Corporation Finance C&DI 133.04 Securities Act Rules (Jan. 26, 2009), available at https://www.sec.gov/divisions/corpfin/guidance/securitiesactrules-interps.htm.

[53] 15 U.S.C. § 77k.

[54] 15 U.S.C. § 77l.

have been few cases of private litigation alleging Securities Act liability as a result of offers and sales using Form S-8, and Form S-8 has not protected investors against companies subjected to Commission enforcement actions against the abuse of Form S-8 to register offers to "consultants" and "advisors" for market-making and capital-raising rather than compensation.[55] It seems that compensatory benefit plan participants do not rely on Form S-8 for investor protections, and so would not be negatively affected in that respect if reporting companies made compensatory offers and sales using Rule 701 instead.

Shares acquired pursuant to a registration statement on Form S-8 are not classified as "restricted securities" for purposes of Rule 144[56] under the Securities Act, and thus sales under the Rule 144 safe harbor can proceed without the need to satisfy the holding period under Rule 144(d).[57]

Advantages of Offerings Under Rule 701.

One advantage of allowing reporting companies to use Rule 701 is that it would eliminate the current administrative burden of filing Form S-8 registration statements. In addition to the administrative burdens involved in the actual filing as discussed above, a reporting company filing a Form S-8 must comply with administrative burdens after filing. The company must deliver a prospectus to the plan participants, and track the number of shares sold under Form S-8, which can be prone to error with regard to stock plans providing for different share costs for different types of awards and can be especially onerous for offerings involving Section 401(k) and similar plans, particularly those that offer a unitized company stock fund as an investment option. Offerings under plans that purchase shares on the open market to cover participant elections can be particularly difficult to track.

Allowing reporting companies to rely on Rule 701 instead of Form S-8 to make compensatory offerings and sales would also eliminate the seeming contradiction that currently exists: Whereas a non-reporting company that is not otherwise required to file financial and operational disclosures can sell up to $10 million of its securities to service providers without providing any disclosure beyond the plan documents, a reporting company that is required to file such disclosures must file a registration statement and provide a prospectus in order to sell its securities to service providers under otherwise similar situations.

Another advantage to providing the Rule 701 exemption to reporting companies as an alternative to Form S-8 registration is that it could eliminate an administrative burden currently borne by companies that are planning an initial public offering ("**IPO**") and the implementation of an employee stock purchase plan ("**ESPP**") that starts on the date of their IPO. Due to the Commission Staff's view that a decision to enroll in an ESPP is an investment decision that requires that the securities be registered on Form S-8, even when employees can withdraw from the ESPP prior to purchasing stock,[58] such companies cannot solicit employee to enroll in their ESPPs until they IPO on Form S-1, and then must file a Form S-8 for the ESPP that incorporates financial statements in their S-1. As a result, companies implementing an ESPP that starts at IPO automatically enroll all of their eligible employees in their ESPPs, and then have employees withdraw from or confirm their enrollment before the first purchase is made under the ESPPs. If reporting companies could rely on Rule 701 instead of Form S-8, companies could solicit employee enrollment in ESPPs prior to their IPOs, and cover the subsequent issuance of shares purchased through the ESPP without having to file a registration statement.

Although Rule 701 lacks the Securities Act protections against material misstatements or omissions that Form S-8 securities registration provides, plan participants can rely on Rule 10b-5 of the Exchange Act for protection against fraud related to the offers and sales of securities pursuant to Rule 701. Furthermore, compensatory offers and sales are less likely to be fraudulent than those for capital-raising or market-making, given that these offers and sales are made to parties with whom companies have ongoing, mutually beneficial work relationships.

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[55] *See* Keith Higgins, Ropes & Gray LLP *Is It Time to Retire Form S-8?,* 31 INSIGHTS 16, 18–9 (September 2017).

[56] 17 CFR 230.144; *cf.* Rule 701(g) [17 CFR 230.701(g)].

[57] 17 CFR 230.144(d).

[58] *See* Employee Benefit Plans Release at Section II.A.5.a.

If the Commission were to extend the Rule 701 exemption to reporting companies, it could limit the exemption to reporting companies that are current in their Section 12 or Section 15(d) filings under the Securities Act so that plan participants would be able to access current financial and operational information. The Commission would not need to impose Rule 701(e) disclosure requirements to sale by reporting companies, because such companies already file financial statements consistent with applicable local regulations, whether those are of the United States or foreign jurisdictions.

We do not believe that it is necessary for the Commission to subject reporting companies using the Rule 701 exemption to the 90-day resale restriction and offering amount limits that apply to non-reporting companies, given that reporting companies provide more disclosures on which the market can rely to make investment decisions.

Lastly in support of the Commission allowing reporting companies to make offers and sales of securities under Rule 701 rather than under a Form S-8 registration, we note that although companies do not have to pay filing fees to use Rule 701 as they do to register securities under Form S-8, Form S-8 registration filing fees comprise a small part of all filing fees collected by the Commission.[59]

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We appreciate the opportunity to participate in this process, and would be pleased to discuss our comments or any questions the Commission may have with respect to this letter. Any questions about this letter may be directed to Kyoko Takahashi Lin, Jean McLoughlin, Veronica Wissel and Gregory Hughes at 212-450-4000.

Very truly yours,

Davis Polk & Wardwell LLP

DAVIS POLK & WARDWELL LLP

[59] *See supra* note 55 at 21.