

**TITLE 12 TRADE, COMMERCE AND BANKING**  
**CHAPTER 11 SECURITIES**  
**PART 9 STANDARDS APPLICABLE TO REGISTERED OFFERINGS**

**12.11.9.1 ISSUING AGENCY:** Regulation and Licensing Department - New Mexico Securities Division.  
[12.11.9.1 NMAC - N, 1-1-2010]

**12.11.9.2 SCOPE:** All persons, whether natural or legal entities, that transact business in New Mexico as a broker-dealer, an investment adviser or an issuer of securities, and their representatives and agents.  
[12.11.9.2 NMAC - N, 1-1-2010]

**12.11.9.3 STATUTORY AUTHORITY:** Section 58-13C-605A NMSA 1978 authorizes the director to adopt, amend and repeal rules necessary or appropriate to carry out the provisions of the New Mexico Uniform Securities Act, Sections 58-13C-101 to 701 NMSA 1978, hereinafter referred to in this Chapter 11 as the “New Mexico Uniform Securities Act”.  
[12.11.9.3 NMAC - N, 1-1-2010]

**12.11.9.4 DURATION:** Permanent.  
[12.11.9.4 NMAC - N, 1-1-2010]

**12.11.9.5 EFFECTIVE DATE:** January 1, 2010, unless a later date is cited at the end of a section.  
[12.11.9.5 NMAC - N, 1-1-2010]

**12.11.9.6 OBJECTIVE:** To implement new rules and revise existing rules to better reflect the realities of current financial, commercial and regulatory principles and practices affecting the securities markets.  
[12.11.9.6 NMAC - N, 1-1-2010]

**12.11.9.7 DEFINITIONS:**

**A. General:** The definitions in this section apply to issuers and promoters of such issuers, organized as limited liability companies, limited partnerships, limited liability partnerships or other legal entities, as appropriate, even though 12.11.9 NMAC refers only to corporate entities and their promoters.

**B. Definitions:** The definitions contained in this section apply to the terms used in 12.11.9 NMAC, except as otherwise provided.

(1) “**Adjusted net earnings**” are the issuer's net earnings after charges for interest and dividends, adjusted on a pro forma basis to reflect:

(a) the elimination of any required charges for debt, debt securities or preferred stock that are to be redeemed or retired from the proceeds derived from the public offering of preferred stock;

(b) the effect of any acquisitions or capital expenditures that were made by the issuer after its last fiscal year, or which are proposed or required to be made during the current fiscal year, which materially affect the issuer's net earnings;

(c) the effect of any charges or dividends on debt, debt securities or preferred stock issued after the issuer's last fiscal year;

(d) the effect of any charges or dividends on debt, debt securities or preferred stock that were issued during the issuer's last fiscal year, but which were outstanding for only a portion of such fiscal year, calculated as if charges or dividends, such debt, debt securities or preferred stock had been outstanding for the entire fiscal year; and

(e) the effect of any other material changes to an issuer's future net earnings.

(2) An “**affiliate**” is a person who, directly or indirectly, controls, is controlled by, or is under common control with the person specified herein.

(3) “**Aggregate revenues**” is the aggregate amount of revenues a promotional or development stage company has received within the last three consecutive fiscal years immediately preceding the public offering plus revenues received during the period covered by any interim period financial information included in the prospectus. Revenues from interest and extraordinary items are to be excluded.

(4) An “**associate**”, when used to indicate a relationship with a person, includes:

(a) corporations or legal entities, other than the issuer or majority-owned subsidiaries of the issuer, of which a person is an officer, director, partner or a direct or indirect legal or beneficial owner of five percent or more of any class of equity securities;

(b) trusts or other estates in which a person has a substantial beneficial interest or for which a person serves as a trustee or in a similar capacity; and

(c) a person's spouse and relatives, by blood or by marriage, if the person is a promoter of the issuer, its subsidiaries, its affiliates or its parent.

(5) "**Average promotional price**" is the average per share price paid for promotional shares and other shares issued prior to the public offering which are of the same class of shares being offered in the public offering as determined by reference to the audited financial statements of the issuer included in the prospectus.

(6) "**Cash analysis**" is the issuer's net cash provided by operating activities as reflected on the statement of cash flows and presented in conformity with generally accepted accounting principles. If debt securities are to be redeemed or retired from the proceeds from the public offering, a pro forma adjustment for the elimination of the related interest charges, net of applicable income taxes, must be made.

(7) "**Control**" is the power to direct or influence the direction of the management or policies of a person, directly or indirectly, through the ownership of voting securities, by contract or otherwise.

(8) "**Equity securities**" include shares of common stock or similar securities and convertible securities, warrants, options or rights that may be converted into, or exercised to purchase, shares of common stock or similar securities.

(9) An "**escrow agent**" is a financial institution whose principal place of business and domicile are in the United States. It may not be affiliated with the issuer, its promoters or associates. A financial institution may not be disallowed to act as an escrow agent merely because the issuer, its promoters or associates are customers thereof. An escrow agent may also include an attorney or certified public accountant, provided that the attorney or certified public accountant is not affiliated with the issuer, its promoters or associates, is licensed to do business in the state in which they practice and can demonstrate that they are adequately insured or can provide a fidelity bond.

(10) An "**impoundment agent**" is a financial institution that is domiciled and whose principal place of business is located in the United States and whose deposits are insured by the FDIC.

(11) An "**independent director**" is a member of issuer's board of directors who:

(a) is not an officer or employee of the issuer, its subsidiaries or their affiliates or associates and has not been an officer, or employee of the issuer, its subsidiaries, or their affiliates or associates within the last two years;

(b) is not a promoter as defined in Paragraph (15) of Subsection B of this section; and,

(c) does not have a material business or professional relationship with the issuer or any of its subsidiaries, affiliates or associates; for purposes of determining whether or not a business or professional relationship is material, the gross revenue derived by the independent director from the issuer, its subsidiaries, its affiliates and associates shall be deemed material per se if it exceeds five percent of the independent director's:

(i) annual gross revenue derived from all sources during either of the last two years; or

(ii) net worth, on a fair market value basis.

(12) "**Lock-in agreement**" is an agreement between an issuer and persons who hold promotional shares wherein, those persons agree, as a condition of registration, not to sell, pledge, hypothecate, assign, grant any option for the sale of, or otherwise transfer or dispose of, whether or not for consideration, directly or indirectly, promotional shares and all certificates representing stock dividends, stock splits, recapitalizations and other capital changes, that are granted to or received by the security holder for the period specified in the lock-in agreement.

(13) "**Net earnings**" are the issuer's after-tax earnings that are derived from its normal operations, exclusive of extraordinary and nonrecurring items, determined according to generally accepted accounting principles consistently applied.

(14) A "**person**" is an individual, a corporation, a limited liability company, a partnership, a limited liability partnership, an association, a joint-stock company, a trust, an unincorporated organization, a government or a political subdivision of a government or any other legal entity.

(15) A "**promoter**" may include:

(a) a person who, alone or in conjunction with one or more persons, directly or indirectly, took the initiative in founding or organizing the issuer or controls the issuer;

(b) a person who, directly or indirectly, receives as consideration for services or property rendered, five percent or more of any class of the issuer's equity securities or five percent or more of the proceeds from the sale of any class of the issuer's equity securities;

(c) a person who receives securities or proceeds solely as underwriting compensation, is excluded from the definition of promoter if that person falls outside the definition of Subparagraphs (a), (d) and (e) of this paragraph;

(d) a person who is an officer or director of the issuer or anyone who legally or beneficially owns, directly or indirectly, five percent or more of any class of the issuer's equity securities; and

(e) a person who is an affiliate or an associate of a person specified in Subparagraphs (a), (b) and (d) of this paragraph.

(16) “**Promoters’ equity investment**” is the total of cash and tangible assets that has been contributed by the promoters to the issuer, provided that the value of the tangible assets is accepted by the director. Promoters’ contributions of intangible assets may be considered as promoters’ equity investment provided that the value thereof has been accepted by the director. Promoters’ equity investment may be adjusted by the issuer’s earned surplus immediately prior to the public offering.

(17) A “**promotional or development stage company**” may include an issuer who is not listed on the New York stock exchange, the American stock exchange or the NASDAQ national market system, and whose annual net earnings for each of the last two consecutive fiscal years or whose average annual net earnings for the last five fiscal years prior to the public offering have been less than five percent of the aggregate public offering.

(18) “**Promotional shares**” are equity securities that are to be issued or were issued:

(a) by an issuer which is a promotional or development stage company, to promoters for cash or other consideration, including services rendered, patents, copyrights and other intangibles (provided that the value thereof has been accepted by the director), that will be or was less than 85 percent of the proposed public offering price; or

(b) within three years prior to the filing of the registration statement to promoters for cash or other consideration, including services rendered, patents, copyrights and other intangibles (provided that the value thereof has been accepted by the director), that will be or was less than 85 percent of the proposed public offering price by a company which is not a promotional or development stage company.

(19) “**Public offering price**” is the per share price at which a promotional or development stage company proposes to offer equity securities to the public.

(20) An “**unaffiliated institutional investor**” is:

(a) an unaffiliated bank or unaffiliated savings and loan company;

(b) an unaffiliated investment company registered under the Investment Company Act of 1940;

(c) an unaffiliated business development company as defined in Section 2(a)(48) of the Investment Company Act of 1940;

(d) an unaffiliated small business investment company licensed by the U.S. small business administration under Section 301 of the Small Business Investment Act of 1958;

(e) an unaffiliated employee benefit plan, within the meaning of Title I of the Employee Retirement Income Security Act of 1974, and state and local government employees retirement and pension plans;

(f) an unaffiliated insurance company;

(g) an unaffiliated trust company;

(h) an unaffiliated private business development company, as defined in Section 202(a)(22) of the Investment Advisers Act of 1940, or a comparable business entity that is engaged as a substantial part of its business in the purchase and sale of securities, and which will own less than 20 percent of the issuer’s securities upon completion of the public offering; or

(i) an unaffiliated qualified purchaser as defined under the National Securities Markets Improvement Act of 1996.

(21) An “**underwriter**” is any person who has agreed with the issuer or other person on whose behalf a distribution is to be made to:

(a) purchase securities for distribution;

(b) distribute securities for or on behalf of the issuer or other person; or

(c) manage or supervise a distribution of securities for or on behalf of the issuer or other

person.

[12.11.9.7 NMAC - Rp, 12 NMAC 11.4.8.1, 1-1-2010]

**12.11.9.8 ADOPTION OF NASAA STATEMENTS OF POLICY FOR REGISTRATION OF CERTAIN TYPES OF SECURITIES:** In order to promote uniform regulation, the director adopts the following NASAA statements of policy set out in CCH NASAA reports published by commerce clearing house. An offering

being registered pursuant to Sections 303 and 304 of the New Mexico Uniform Securities Act must comply with the requirements of said statements of policy or policies as adopted and as revised in subsequent amendments.

- A. Asset-backed securities.
- B. Cattle feeding programs.
- C. Commodity pool programs.
- D. Equipment programs.
- E. Mortgage programs.
- F. Oil and gas programs.
- G. Omnibus programs.
- H. Real estate investment trusts.
- I. Real estate programs.

[12.11.9.8 NMAC - Rp, 12 NMAC 11.4.10, 1-1-2010]

#### **12.11.9.9 IMPOUNDMENT OF PROCEEDS:**

A. When an impoundment agreement (“agreement”) is necessary, the proceeds from the sale of the securities must be deposited in an interest bearing escrow or trust account with an impoundment agent. The impoundment agent may not be affiliated with the issuer, its affiliates, its officers or directors, the underwriter or any promoter.

B. The agreement:

(1) a signed copy of the agreement must be filed with the director and shall become part of the registration statement;

(2) the agreement must be signed by an officer of the issuer, an officer of the underwriter (if applicable) and an officer of the impoundment agent; the aforesaid individuals must have the authority to sign such documents;

(3) the agreement shall provide that the impounded proceeds (proceeds) are not subject to claims by creditors of the issuer, affiliates, associates or underwriters until the proceeds have been released to the issuer pursuant to the terms of the agreement;

(4) a summary of the principal terms shall be included in the registration statement; and

(5) the agreement shall provide that the director has the right to inspect and make copies of the records of the impoundment agent at any reasonable time wherever the records are located.

C. The impoundment agent shall notify the director in writing upon the release of the proceeds. If the proceeds are insufficient to meet the minimum requirements within the time prescribed by the agreement:

(1) the impoundment agent must release and return the proceeds directly to the investors; and

(2) the proceeds shall be released and returned to the investors without deduction for expenses including impoundment agent fees and shall include a pro rata share of interest earned.

D. If a person who is an underwriter or an officer, director, promoter, affiliate or an associate of the issuer purchases securities that are a part of the public offering being sold pursuant to the registration statement and if the proceeds from that purchase are used for the purpose of completing the impoundment requirements imposed under this rule, the following conditions shall be met:

(1) the persons are purchasing the securities on the same terms as unaffiliated public investors;

(2) the prospectus contains a disclosure that such persons may purchase securities of the issuer for purposes of completing the impoundment requirements imposed by this rule; and

(3) all securities so purchased will neither be defined as “promotional shares” nor be a part of the calculation of the promotional shares subject to escrow under 12.11.9.13 NMAC; however, all such securities shall be immediately subject to the escrow/lock-up provisions of 12.11.9.13 NMAC.

[12.11.9.9 NMAC - Rp, 12 NMAC 11.4.8.2, 1-1-2010]

#### **12.11.9.10 LOANS AND OTHER MATERIAL AFFILIATED TRANSACTIONS:**

A. Where there have been or will be loans and other material affiliated transactions as described in this section, the offer or sale of securities may be disallowed by the director unless the issuer has, and represents in the prospectus or offering document that it will maintain, at least two independent directors on its board of directors.

B. The offer or sale of securities may be disallowed by the director if the issuer or its affiliates will have loans outstanding after the offering or intends to make loans to or loan guarantees on behalf of its promoters, other than:

(1) advances to officers, directors and employees for travel, business expenses and similar ordinary operating expenditures;

(2) loans or loan guarantees made for the purchase of an issuer's securities by its officers, directors and employees, and loans for relocation of officers, directors and employees, provided the loans or loan guarantees that are ongoing were approved by a majority of the independent directors of the issuer's board of directors who did not have an interest in the transactions and who had access, at the issuer's expense, to issuer's or independent legal counsel; or

(3) loans made by an issuer or its affiliates whose primary business is that of making loans, provided that:

(a) the loans will be evidenced by promissory notes naming the lender as payee;

(b) the loans will bear interest at rates which are comparable to those normally charged by other commercial lenders for similar loans made in the lender's locale;

(c) the loans will be repaid pursuant to appropriate amortization schedules and contain default provisions comparable to those normally used by other commercial lenders for similar loans made in the lender's locale;

(d) the loans will be made only if credit reports and financial statements show the loans to be collectible and the borrowers are satisfactory credit risks in light of the nature and terms of the loans and other circumstances;

(e) the loans meet the loan policies normally used by other commercial lenders for similar loans made in the lender's locale;

(f) the purposes of the loans and the disbursements of proceeds will be reviewed and monitored in a manner comparable to that normally used by other commercial lenders for similar loans made in the lender's locale; and

(g) the loans will not violate the requirements of any banking or other financial institutions regulatory authority.

**C.** Except for loans described in Subsection B of this section, all loans existing at the time of the application for registration shall be repaid in full prior to the offering. The director may waive this requirement if:

(1) repayment of the loans will be made pursuant to appropriate amortization schedules; or

(2) any portion of the offering is made on behalf of a promoter and the promoter undertakes to immediately repay the loans from the proceeds of the offering.

**D.** The offer or sale of securities may be disallowed by the director if the issuer or its affiliates have engaged in other material transactions with promoters unless the prospectus discloses the terms of the transactions and indicates whether such terms were as favorable to the issuer or its affiliates as those generally available from unaffiliated third parties, and:

(1) the transaction is ratified by a majority of the issuer's independent directors who did not have an interest in the transactions and who had access, at the issuer's expense, to issuer's or independent legal counsel; or

(2) for transactions which were entered into and when there were less than two such disinterested independent directors the prospectus discloses that the issuer lacked sufficient disinterested independent directors to ratify the transactions at the time the transactions were initiated.

**E.** The issuer shall disclose in the prospectus or offering document whether or not it or its affiliates have made or will make loans to, have made or will make loan guarantees on behalf of, or have engaged or will engage in material transactions with promoters, and the terms and details relating thereto. If material affiliated transactions or loans have been made, or may be made, the director may require the following representations to appear in the prospectus or offering document:

(1) all future loans and other material affiliated transactions will be made or entered into on terms that are no less favorable to the issuer than those that can be obtained from unaffiliated third parties; and

(2) all future loans and other material affiliated transactions, and any forgiveness of loans, must be approved by a majority of the issuer's independent directors who do not have an interest in the transactions and who had access, at the issuer's expense, to issuer's or independent legal counsel.

**F.** The issuer and its officers and directors should consider their due diligence and other obligations to affirmatively demonstrate a reasonable basis for the representations in Subsections D and E of this section. In particular, they should consider whether the representations in Paragraph (1) of Subsection D and Paragraph (2) of Subsection E of this section should be embodied in the issuer's charter or by-laws.

**G.** An issuer that engages in loans and other material affiliated transactions covered by Paragraph (2) of Subsection B, Paragraph (1) of Subsection D and Paragraph (2) of Subsection E of this section must have at least two independent directors on its board of directors. In the event the issuer has only two independent directors on its board or directors, both independent directors must be disinterested in and approve loans and other material

transactions covered by Paragraph (2) of Subsection B, Paragraph (1) of Subsection D and Paragraph (2) of Subsection E of this section.

[12.11.9.10 NMAC - Rp, 12 NMAC 11.4.8.3, 1-1-2010]

**12.11.9.11 OPTIONS AND WARRANTS:**

**A.** Options or warrants may be issued to underwriters as compensation in connection with a public offering provided those options or warrants comply with the requirements of 12.11.9.15 NMAC, underwriting expenses, underwriter's warrants, selling expenses and selling security holders.

**B.** Options or warrants may be granted to unaffiliated institutional investors in connection with loans if:

- (1) the options or warrants are issued contemporaneously with the issuance of the loan;
- (2) the options or warrants are granted as the result of bona fide negotiations between the issuer and unaffiliated institutional investor;
- (3) the exercise price of the options or warrants is not less than the fair market value of the issuer's shares of common stock underlying the options or warrants on the date that the loan was approved; and
- (4) the number of shares issuable upon exercise of the options or warrants multiplied by the exercise price thereof does not exceed the face amount of the loan.

**C.** Options or warrants may be issued in connection with acquisitions, reorganizations, consolidations or mergers if:

- (1) they are issued to persons who are unaffiliated with the issuer; and
- (2) the earnings of the issuer at the time of issuance and after giving effect to the acquisition, reorganization, consolidation or merger would not be materially diluted by the exercise of the options or warrants.

**D.** Options and warrants may not be issued at an exercise price of less than 85 percent of fair market value of the issuer's underlying shares of common stock on the date of grant. The issuer, its officers and directors should consider the advisability of obtaining a concurrent appraisal by a qualified independent appraiser of the value of the shares of common stock at the time of issuance as evidence of the fair market value.

**E.** The total number of options and warrants issued or reserved for issuance at the date of the public offering, excluding those options and warrants that were issued or reserved for issuance pursuant to Subsections C and D of this section, may not, for one year following the effective date of the offering, exceed fifteen percent of the issuer's shares of common stock outstanding at the date of the public offering plus the number of shares of common stock being offered that are firmly underwritten or, in the case of offerings not firmly underwritten, the number of shares of common stock required to be sold in order to meet the minimum offering amount. In calculating the number of options and warrants, the following are excluded:

- (1) options and warrants that were issued or reserved for issuance pursuant to Subsections B, C and D of this section;
- (2) options and warrants that were issued, or reserved for issuance, to employees or consultants who are not promoters, in connection with an incentive stock option plan qualified under Section 422 of the Internal Revenue Code; and
- (3) options and warrants that are exercisable at or above the public offering price.

**F.** No options or warrants issued and outstanding at the date of the public offering, excluding those options and warrants issued pursuant to an incentive stock option plan qualified under Section 422 of the Internal Revenue Code, may be exercisable more than five years from the date of the public offering.

**G.** If the number of options and warrants that are issued and outstanding or reserved for issuance is material, the final offering circular shall disclose the potential dilutive effects of such options and warrants.

[12.11.9.11 NMAC - Rp, 12 NMAC 11.4.8.4, 1-1-2010]

**12.11.9.12 PROMOTER'S EQUITY INVESTMENT:** A public securities offering by a promotional or development stage company may be disallowed by the director if the promoters' equity investment is less than:

- A.** ten percent of the first \$1,000,000 of the aggregate public offering;
- B.** seven percent of the next \$500,000 of the aggregate public offering;
- C.** five percent of the next \$500,000 of the aggregate public offering; and
- D.** two and one-half percent of the balance exceeding \$2,000,000 of the aggregate public offering, which may include items submitted by the promoter to meet this requirement whose value has been accepted by the director.

[12 NMAC 11.4.12.4, 12-30-95; 12 NMAC 11.4.8.5, 5-1-99; 12.11.9.12 NMAC - Rp, 12 NMAC 11.4.8.5, 1-1-2010]

### **12.11.9.13 PROMOTIONAL SHARES:**

**A. Escrow of promotional shares:** The director may require that some or all of the promoters deposit some or all of their promotional shares into an escrow account (“escrow”) with an escrow agent according to the terms of an escrow agreement (“agreement”) as a condition to registering a public offering of equity securities. The promoters, who are required to deposit some or all of their promotional shares into escrow, are hereinafter collectively referred to as depositors. The director may, at his discretion, require a lock-in agreement on substantially the same terms and conditions as an agreement.

#### **B. Release of promotional shares.**

(1) The escrow agent shall release the promotional shares in the following manner, if:

- (a) the issuer's aggregate revenues are:
  - (i) \$500,000 or more, provided that neither the auditor’s report nor any footnote to the issuer’s latest audited financial statement contains an opinion or statement regarding the ability of the issuer to continue as a going concern; beginning one year from the date the offering is declared effective, two and one-half percent of promotional shares held in escrow may be released each quarter pro rata among the depositors; all remaining promotional shares shall be released from escrow on the second anniversary from the date the offering is declared effective; or
  - (ii) less than \$500,000; beginning two years from the date the offering is declared effective, two and one-half percent of promotional shares held in escrow may be released each quarter pro rata among the depositors; all remaining promotional shares shall be released from escrow on the third anniversary from the date the offering is declared effective;
- (b) the public offering has been terminated and no securities were sold pursuant thereto; or
- (c) the public offering has been terminated and all of the gross proceeds that were derived therefrom have been returned to the public investors.

(2) In the event of a dissolution, liquidation, merger, consolidation, reorganization, sale or exchange of the issuer's assets or securities (including by way of tender offer), or any other transaction or proceeding with a person who is not a promoter which results in the distribution of the issuer's assets or securities (“distribution”), while this agreement remains in effect, the depositors agree that:

(a) all holders of the issuer’s equity securities will initially share on a pro rata, per share basis in the distribution, in proportion to the amount of cash or other consideration that they paid per share of equity securities (provided that the director has accepted the value of the other consideration), until the public shareholders have received, or have had irrevocably set aside for them, an amount that is equal to 100 percent of the public offering’s price per share times the number of shares of equity securities that they purchased pursuant to the public offering and which they still hold at the time of the distribution, adjusted for stock splits, stock dividends, recapitalizations and the like;

(b) all holders of the issuer’s equity securities shall thereafter participate on an equal, per share basis times the number of shares of equity securities they hold at the time of the distribution, adjusted for stock splits, stock dividends, recapitalizations and the like; and

(c) a distribution may proceed on lesser terms and conditions than the terms and conditions stated in Paragraph (1) of this subsection if a majority of the equity securities that are not held by promoters or their associates or affiliates, vote or consent by consent procedure, to approve the lesser terms and conditions at a special meeting called for that specific purpose.

(3) In the event of a dissolution, liquidation, merger, consolidation, reorganization, sale or exchange of the issuer’s assets or securities (including by way of tender offer) or any other transaction or proceeding with a person who is a promoter, which results in a distribution while this agreement remains in effect, the depositors’ promotional shares shall remain in escrow subject to the terms of the agreement.

(4) In the event securities in the escrow become “covered securities” as defined in the National Securities Markets Improvement Act of 1996, all securities in the escrow shall be released.

#### **C. Documentation regarding the termination of the escrow agreement or the release of promotional shares or both.**

(1) A request for the release of any of the promotional shares from escrow shall be in writing and be forwarded to the escrow agent.

(2) The issuer shall provide to the escrow agent the documentation showing that the requirements of Subsection B of this section have been met.

(3) The escrow agent shall terminate the agreement, or release some or all of the promotional shares from escrow, or both, if all the applicable provisions of the agreement have been satisfied. The escrow agent shall

maintain all records relating to the agreement for a period of three years following the termination of the agreement. Copies of all records retained by the escrow agent shall be forwarded to the director promptly upon written request.

**D. Restrictions on the transfer, sale or disposal of promotional shares.**

(1) Promotional shares may be transferred by will, the laws of descent and distribution, operation of law or any court of competent jurisdiction and proper venue.

(a) The promotional shares of a deceased depositor may be hypothecated to pay the expenses of the deceased depositor's estate provided that the hypothecated promotional shares shall remain subject to the terms of the agreement.

(b) No promotional shares may be transferred, sold or disposed of ("transferred") until the escrow agent has received a written statement signed by the proposed transferee ("transferee") which states that the transferee has full knowledge of the terms of the agreement, the transferee accepts the promotional shares subject to the terms of the agreement, and the transferee realizes that the promotional shares shall remain in escrow until they are released pursuant to Subsection B of this section.

(2) With the exception of Subparagraph (a) of Paragraph (1) of this subsection, promotional shares may not be pledged to secure a debt.

(3) Promotional shares may be transferred by gift to the depositor's family members, provided that the promotional shares shall remain subject to the terms of the agreement.

(4) With the exception of Paragraph (1) of this subsection, no promotional shares, any interest therein or any right or title thereto, may be transferred.

(5) In the case of a self-underwritten offering, notwithstanding the provisions of Paragraph (1) of Subsection B of this section, promoters shall be prohibited from selling any of the promotional shares that are not subject to escrow during the time that the issuer is offering its securities to the public.

**E. Terms of the escrow.**

(1) Except as noted in Subparagraph (c) of Paragraph (2) of Subsection B, depositors shall have the same voting rights as shareholders who purchased equity securities pursuant to the public offering ("public shareholders").

(2) All certificates representing stock dividends and shares resulting from stock splits of escrowed shares, recapitalizations and the like that are granted to or received by depositors while their promotional shares are held in escrow shall be deposited with and held by the escrow agent subject to the terms of the agreement. Any cash dividends that are granted to or received by depositors while their promotional shares are held in escrow, shall be deposited with and held by the escrow agent subject to the terms of the agreement. The escrow agent shall invest such cash dividends as directed by the depositors. The cash dividends and any interest earned thereon will be disbursed in proportion to the number of shares released from the escrow.

(3) Equity securities that are received by depositors as the result of the conversion or exercise of convertible securities, warrants, options or rights to purchase common stock or similar securities, while their promotional shares are in escrow, shall be deposited with and held by the escrow agent subject to the terms of the escrow.

(4) A summary of the agreement shall be included in the prospectus and subsequent amendments thereto, annual reports to shareholders, proxy statements and other disclosure materials that are used to make investment decisions until the public offering has been terminated.

(5) The escrow agent shall be entitled to reasonable compensation from the issuer for its services as set forth in the agreement. If the escrow agent is required to render additional services that are not expressly provided for therein, or if it is made a party to or intervenes in any action, suit or proceeding pertaining to the agreement, it shall be entitled to receive reasonable compensation from the issuer and the depositors. If additional services are provided, the escrow agent, after giving written notice to the depositors and issuer, may deduct reasonable compensation from any cash dividends, interest and other offering proceeds that are being held by it for distribution pursuant to the agreement.

(6) The issuer and the depositors shall hold the escrow agent harmless from, and indemnify it for, any cost or liability regarding any administrative proceeding, investigation, litigation, interpretation, implementation or interpleading relating to the agreement, including the release of promotional shares and the disbursement of dividends, interest or other offering proceeds, unless the cost or the liability arises from the escrow agent's failure to abide by the terms of the agreement.

(7) The agreement shall be binding upon the depositors, their heirs and assignees, and upon the issuer and escrow agent and their successors.

(8) Except for the escrow agent's compensation and indemnification provisions which shall survive until they are satisfied, the agreement will be terminated when all of the promotional shares have been released or the issuer's equity securities or the assets have been distributed pursuant to the agreement.  
[12.11.9.13 NMAC - Rp, 12 NMAC 11.4.8.6, 1-1-2010]

#### **12.11.9.14 SPECIFICITY IN USE OF PROCEEDS:**

**A.** A registration statement not complying with the requirements of this section may be denied registration by the director.

**B.** The issuer's prospectus shall disclose in a tabular form for both the minimum and maximum amounts proposed, if applicable, the percentages and dollar amounts of the following:

- (1) the estimated cash proceeds to be received by the issuer from the offering;
- (2) the purposes for which the proceeds are to be used by the issuer;
- (3) the amount to be used for each purpose; and
- (4) the order or priority in which the proceeds will be used for the purposes stated.

**C.** Additionally, the issuer's prospectus shall disclose:

- (1) the amounts of any funds to be raised from other sources to achieve the purposes stated, whether the sources are firm or contingent and any contingencies;
- (2) the sources of any such funds, whether the sources are firm or contingent and any contingencies;
- (3) if any part of the proceeds is to be used to acquire any property (including goodwill) other than in the ordinary course of business, the names and addresses of the vendors, the purchase price, the names of any persons who have received commissions in connection with the acquisition, and the amounts of any such commissions and any other expense in connection with the acquisition (including the cost of borrowing money to finance the acquisition); and
- (4) the amount and basis for any proceeds used to pay indebtedness, including unpaid salaries, to promoters.

**D.** The issuer normally may not reserve more than 15 percent proceeds for working capital or general corporate purposes (or for any other unspecified use). In the event the issuer's business plans require greater flexibility in the use of unspecified proceeds, the issuer must:

- (1) disclose all potential uses of such proceeds with qualifying language that such uses may be subject to change; and
- (2) indicate the specific circumstances leading to reallocation and the potential areas of reallocation.

**E.** The issuer must demonstrate that the offering proceeds, together with all other sources of financing currently available to the issuer, are sufficient to sustain the issuer's proposed activities. If such proceeds are insufficient to sustain the issuer's activities for at least 12 months following the offering, the issuer must provide the appropriate risk disclosure in the prospectus.

**F.** In the event the offering is not firmly underwritten, the issuer must set a minimum amount of proceeds to be raised consistent with the business plan set forth in the prospectus. These proceeds must be impounded until such minimum amount is reached. In the event money is impounded in a non-interest bearing account, the prospectus must disclose this fact to investors. Additionally, the prospectus must disclose if officers, directors or other promoters have the right to purchase shares for the purpose of meeting the impound requirements.  
[12.11.9.14 NMAC - Rp, 12 NMAC 11.4.8.7, 1-1-2010]

#### **12.11.9.15 UNDERWRITING EXPENSES, UNDERWRITER'S WARRANTS, SELLING EXPENSES AND SELLING SECURITY HOLDERS:**

**A.** An offer or sale of securities may be disallowed by the director if the underwriting expenses to be incurred exceed 17 percent of the gross proceeds from the public offering.

**B.** Underwriting expenses include, but are not limited to:

- (1) commissions to underwriters or broker-dealers;
- (2) non-accountable fees or expenses to be paid to the underwriters or broker-dealers;
- (3) underwriter's warrants, which shall be valued using the following formula:  $.5 \text{ multiplied by } ((165 \text{ percent of the offering price}) \text{ minus } (\text{the exercise price multiplied by the number of shares offered to the public})) \text{ multiplied by } (\text{the number of shares underlying the warrants divided by the number of shares offered to the public}) \text{ equals Warrant Value}$ ; the value may be reduced by 20 percent if the exercise period of the warrants is extended from one year after the public offering to two years after the public offering and by 40 percent if the exercise period of the warrants is extended from one year after the public offering to three years after the public offering; warrants granted to underwriters are subject to the following restrictions:

- (a) the underwriter is a managing underwriter;
  - (b) the public offering is either a firmly underwritten offering or a “minimum-maximum” offering; options or warrants may be issued in a “minimum-maximum” public offering only if:
    - (i) the options or warrants are issued on a pro rata basis;
    - (ii) the “minimum” amount of securities has been sold;
    - (iii) the exercise price of the warrants is at least equal to the public offering price;
    - (iv) the number of shares covered by underwriter's options or warrants does not exceed ten percent of the shares of common stock actually sold in the public offering;
    - (v) the life of the options or warrants does not exceed a period of five years from the completion date of the public offering;
    - (vi) the options or warrants are not exercisable for the first year after the completion date of the public offering; and
  - (c) options or warrants are not transferred, except:
    - (i) to partners of the underwriter, if the underwriter is a partnership;
    - (ii) to officers and employees of the underwriter, who are also shareholders of the underwriter if the underwriter is a corporation; or
    - (iii) by will, pursuant to the laws of descent and distribution, or by the operation of law;
  - (d) the warrant agreement does not allow for a reduction in the exercise price of the options or warrants resulting from the subsequent issuance of shares by the issuer except where such issuances are pursuant to a:
    - (i) stock dividend or stock split; or
    - (ii) merger, consolidation, reclassification, reorganization, recapitalization or sale of assets;
  - (4) right of first refusal, which shall be valued at 1 percent of the public offering or the amount payable to the underwriter if the issuer terminates the right of first refusal;
  - (5) solicitation fees payable to the underwriter, which shall be valued at the lesser of actual cost or one percent of the public offering if the fees are payable within one year of the offering;
  - (6) financial consulting or financial advisory agreements with an underwriter or any other similar type of agreement or fees, however designated, which shall be valued at actual cost;
  - (7) underwriter's due diligence expenses;
  - (8) payments made either six months prior to or required to be made six months following the public offering to investor relations firms designated by the underwriter; and
  - (9) other underwriting expenses incurred in connection with the public offering of securities as determined by the director.
- C.** Underwriting expenses shall not include financial consulting or financial advisory agreements with the underwriter payable at the time the services are rendered, provided that such agreement was entered into at least twelve months before the registration is filed with the SEC.
- D.** An offer or sale of securities may be disallowed by the director if the direct and indirect selling expenses of the offering exceed 20 percent of the gross proceeds from the public offering.
- E.** Selling expenses include, but are not limited to:
- (1) commissions to underwriters or broker-dealers;
  - (2) non-accountable fees or expenses to be paid to the underwriters or broker-dealers;
  - (3) auditors' and accountants' fees;
  - (4) legal fees;
  - (5) the cost of printing prospectuses, circulars and other documents required to comply with securities laws and regulations;
  - (6) charges of transfer agents, registrars, indenture trustees, escrow holders, depositories, engineers, appraisers and other experts;
  - (7) the cost of authorizing and preparing the securities, including issue taxes and stamps;
  - (8) financial consulting or financial advisory agreements with an underwriter or any similar type agreement or fees, however designated, which shall be valued at actual cost, excluding financial and consulting agreements which are entered into at least 12 months before the registration is filed with the SEC;
  - (9) payments made either six months prior to or required to be made six months following the public offering to investor relations firms designated by the underwriter; and
  - (10) other selling expenses incurred in connection with the public offering of securities as determined by the director.

**F.** A public offering or sale of securities that includes selling security holders offering in aggregate more than ten percent of the securities to be sold in the public offering may be disallowed by the director unless:

(1) selling security holders offering or selling in aggregate more than 10 percent but less than 50 percent of the securities to be sold in the public offering pay a pro rata share of all selling expenses of the public offering, excluding the legal and accounting expenses of the public offering;

(2) selling security holders offering in aggregate more than 50 percent of the securities to be sold in the offering pay a pro rata share of all selling expenses of the public offering; and

(3) the prospectus or offering document discloses the amount of selling expenses which the selling security holders will pay.

**G.** With the exception of underwriter's or broker-dealer's compensation, the provisions of Subsection F of this section shall not apply if the selling security holders have a written agreement with the issuer that was entered into in an arms-length transaction, whereby the issuer has agreed to pay all of the selling security holders' selling expenses.

[12.11.9.15 NMAC - Rp, 12 NMAC 11.4.8.8, 1-1-2010]

**12.11.9.16 UNEQUAL VOTING RIGHTS:** The offer and sale of securities that have less-than-equal voting rights may be deemed to be inconsistent with public investor protection and against public policy by the director unless:

**A.** the securities are given preferential treatment as to dividends and liquidation or the less than equal voting rights are justified to the satisfaction of the director; and

**B.** the terms of the voting rights are prominently disclosed on the cover page of the issuer's offering circular or prospectus.

[12.11.9.16 NMAC - Rp, 12 NMAC 11.4.8.9, 1-1-2010]

**12.11.9.17 UNSOUND FINANCIAL CONDITION:**

**A.** An issuer shall be deemed to be in unsound financial condition if the financial statements contain:

(1) a footnote to the financial statements or an explanatory paragraph in the independent auditor's report regarding the issuer's ability to continue as a going concern; and

(2) at least one of the following, or a similar fact:

(a) an accumulated deficit;

(b) negative shareholder equity;

(c) an inability to satisfy current obligations as they come due; or

(d) negative cash flow (or revenues not being generated by operations).

**B.** If the application for registration contains audited financial statements which were issued more than 90 days from the date of application, the accompanying interim unaudited financial statements are subject to the scrutiny of this section.

**C.** An application for registration by an issuer in unsound financial condition may be denied by the director.

**D.** An application for registration by an issuer in unsound financial condition may be registered by the director if the chief financial officer of the issuer provides pro forma financial data acceptable to the director that:

(1) demonstrate that the issuer's financial condition will improve either as a direct result of the offering proceeds or as a proximate result of the offering proceeds (as part of a long-term business plan);

(2) demonstrate when profitability is expected to occur; and

(3) are supported with documentation of, and the bases for, any assumptions.

**E.** In addition to satisfying the requirements of Subsection D of this section, the issuer must:

(1) include prominent disclosure that the issuer is considered to be in unsound financial condition and that persons should not invest unless they can afford to lose their entire investment; and

(2) disclose the following risk factors, as applicable:

(a) the presence of an explanatory paragraph in the independent auditor's report;

(b) if the issuer has not been generating revenues from operations, the means by which the issuer has been financing its operations;

(c) the amount of any accumulated deficit;

(d) the presence and amount of any negative shareholder's equity; and

(e) the need for future financing.

**F.** Nothing in this section shall prevent the director from imposing net worth standards or limiting the sales of securities to accredited investors in lieu of, or in addition to, the requirements of Subsections D and E of this section. The imposition of these minimal net worth standards does not relieve a dealer from the responsibility of making an independent determination of suitability required under industry standards. Unless the director determines that the risks associated with the offering would require lower standards, public investors shall have the following:

(1) a minimum annual gross income of \$70,000 and a minimum net worth of \$70,000, exclusive of automobile, home and home furnishings; or

(2) a minimum net worth of \$250,000, exclusive of automobile, home and home furnishings.

[12.11.9.17 NMAC - Rp, 12 NMAC 11.4.8.10, 1-1-2010]

#### **12.11.9.18 PREFERRED STOCK:**

**A.** A public offering of preferred stock may be disallowed by the director if the issuer's adjusted net earnings for the last fiscal year or its average adjusted net earnings for the last three fiscal years prior to the public offering were insufficient to pay its fixed charges and preferred stock dividends, whether or not accrued, and to meet the redemption requirements, if applicable, of the preferred stock being offered.

**B.** As an alternative to Subsection A of this section, the director may choose to apply a cash analysis. The director may consider the statement of cash flows if the statement demonstrates that the issuer has had positive "net cash provided by operating activities" for its last fiscal year. The director may request that the issuer submit a financial statement demonstrating an average positive "net cash provided by operating activities" for the last three fiscal years prior to the public offering. In either instance there must be sufficient cash to cover the preferred stock dividend whether or not declared.

**C.** Subsections A and B of this section shall not apply to public offerings of convertible preferred stock that are superior in right to payment of dividends, interest and liquidation proceeds to any convertible debt and preferred stock that are or may be legally or beneficially, directly or indirectly, owned by promoters. The risks of failure to declare or pay dividends and the equity characteristics of the convertible preferred stock must be disclosed in the offering prospectus. An offering of such securities may be reviewed using guidelines for equity offerings.

**D.** If the issuer's net earnings are subject to cyclical fluctuations or if the director deems it necessary for investor protection, the director may require that the issuer establish redemption requirements.

**E.** A public offering of equity securities may be disallowed by the director if the issuer's articles of incorporation authorize its board of directors to issue preferred stock in the future without a vote of the common shareholders unless:

(1) the issuer represents in its prospectus or offering document that it will not offer preferred stock to promoters except on the same terms as it is offered to all other existing shareholders or to new shareholders; or

(2) the issuance of preferred stock is approved by a majority of the issuer's independent directors who do not have an interest in the transaction and who have access, at the issuer's expense, to issuer's or independent legal counsel.

[12.11.9.18 NMAC - Rp, 12 NMAC 11.4.8.11, 1-1-2010]

#### **12.11.9.19 DEBT SECURITIES:**

**A.** The following definitions shall apply to this section.

(1) "**Adjusted cash flow**" is the issuer's cash flow adjusted on a pro forma basis to reflect:

(a) the elimination of interest and fees on debt or debt securities and of cash dividends on preferred stock that are to be retired with the proceeds derived from the offering;

(b) the effect of any acquisitions or capital expenditures that were made by the issuer after its last fiscal year, or which are proposed or required for the current fiscal year, which materially affect the issuer's cash flow;

(c) the effect of interest and fees on debt or debt securities or cash dividends paid after the issuer's last fiscal year;

(d) the effect of any interest and fees or debt securities and of cash dividends on preferred stock or common stock that were issued during the issuer's last fiscal year, as if such debt, debt securities, preferred stock or common stock had been outstanding for the entire fiscal year;

(e) the effect of imputed or deferred charges of zero coupon debt or debt securities for the issuer's last fiscal year and any additional charges on such debt or debt securities issued after the issuer's last fiscal year;

(f) except as provided in Subsection C of this section, the effect of accrued dividends on preferred stock for the issuer's last fiscal year and any additional dividends on such preferred stock issued after the issuer's last fiscal year; and

(g) the effect of any other material changes to the issuer's future cash flow.

(2) "**Cash flow**" is the issuer's after-tax earnings that are derived from its normal operations, exclusive of extraordinary and nonrecurring items, less interest and dividends, plus certain noncash charges against earnings such as depreciation, depletion and amortization, determined according to generally accepted accounting principles consistently applied.

(3) A "**promoter**" may include:

(a) a person who, alone or in conjunction with one or more persons, directly or indirectly, founded or organized the issuer or controls the issuer;

(b) a person who, directly or indirectly, receives as consideration for services or property rendered, five percent or more of any class of the issuer's equity securities or five percent or more of the proceeds from the sale of any class of the issuer's equity securities;

(c) a person who receives securities or proceeds solely as underwriting compensation is excluded from the definition of promoter if that person falls outside of the definitions of Subparagraphs (a), (d) and (e) of Paragraph (3) of this subsection;

(d) a person who is an officer or director of the issuer;

(e) a person who legally or beneficially, directly or indirectly, owns five percent or more of any class of the issuer's equity securities ("five percent shareholder") if that person was in control of the issuer at the time of acquiring five percent of any class of the issuer's equity securities or if that person is in control of the issuer at the time of public offering of the issuer's equity securities; or

(f) a person who is an affiliate or an associate of a person specified in Subparagraphs (a), (b), (c) or (d) of Paragraph (3) of this subsection.

**B.** A public offering of debt securities may be disallowed by the director if the issuer's adjusted cash flow for the last fiscal year or its average adjusted cash flow for the last three fiscal years prior to the public offering was insufficient to cover its fixed charges, meet its debt obligations as they became due, and service the debt securities being offered.

**C.** Notwithstanding Subparagraph (f) of Paragraph (1) of Subsection A of this section, accrued dividends of cumulative preferred stock having a stated interest rate may be excluded from adjusted cash flow at the discretion of the director.

**D.** The director, in the director's sole discretion, may choose not to apply Subsection B of this section to a public offering of convertible securities that are superior in right of payment of interest and liquidation proceeds to any convertible debt that is or may be legally or beneficially, directly or indirectly, owned by promoters. The risks of failure to meet debt service obligations and the equity characteristics of such securities must be disclosed in the prospectus. An offering of such securities may be reviewed using guidelines for equity offerings.

**E.** Unless the director permits otherwise, public offerings of debt securities shall be offered and sold pursuant to a trust indenture ("indenture") which adequately protects the rights of the purchasers. Some of these protections are:

(1) the indenture shall comply with the provisions of the Trust Indenture Act of 1939; this shall be disclosed in the offering document;

(2) the events of default of the indenture shall be disclosed in the offering document;

(3) the trustee shall be provided with adequate reports, including any compliance reports from independent auditors, to allow the trustee to ensure compliance with the indenture;

(4) neither the trustee nor the promoters may be major creditors of the issuer or its affiliates;

(5) the indenture shall provide that upon any consolidation, merger, recapitalization, reorganization, pledge foreclosure, equity or share exchange, conveyance or transfer of the properties and assets of the issuer substantially as an entirety, or any other transaction having a substantially equivalent effect, the successor person shall expressly assume the payment obligations on the debt securities and the duty to perform the covenants of the indenture;

(6) the indenture shall provide that interest will accrue and be paid to the date(s) of redemption or conversion of the debt securities.

**F.** If the issuer's cash flow is subject to cyclical fluctuations or if the director deems it necessary for investor protection, the director may require that the issuer establish a sinking fund or redemption requirements. [12.11.9.19 NMAC - Rp, 12 NMAC 11.4.8.12, 1-1-2010]

### **HISTORY OF 12.11.9 NMAC:**

**Pre-NMAC History:** Material in this part was derived from that previously filed with the commission of public records - state records center and archives:

FID 67-1, Regulation 67-62, General Requirements, filed 5-18-67.

FID 76-1, Order 76-64, Regulation 76-1, Relating to Options Clearing Corporations, filed 3-26-76.

SB Rule 84-1, New Mexico Blue Sky Regulations, filed 9-5-84.

SD Rule 86-5.02, Offering Price, filed 7-11-86.

SD Rule 95-5.02, Selling Expenses and Selling Security Holders, filed 9-27-95.

SD Rule 86-5.03, Options and Warrants, filed 7-11-86.

SD Rule 86-5.04, Cheap Stock, filed 7-11-86.

SD Rule 95-5.04, Promotional Shares, filed 9-27-95.

SD Rule 86-5.05, Insiders Equity, filed 7-11-86.

SD Rule 95-5.24, Impoundment of Proceeds, filed 9-27-95.

SD Rule 95-5.25, Loans and Other Material Affiliated Transactions, filed 9-27-95.

SD Rule 95-5.26, Debt Securities, filed 9-27-95.

### **History of Repealed Material:**

That relevant portion of 12 NMAC 11.4; numbered Subpart 8, Registration of Securities (filed 4-19-99) and Subpart 10, Adoption of NASAA Statements of Policy for Registration of Certain Types of Securities (filed 4-19-99) repealed 1-1-2010.

### **Other History:**

SD Rule 95-5.02, Selling Expenses and Selling Security Holders, filed 9-27-95;

SD Rule 86-5.03, Options and Warrants, filed 7-11-86;

SD Rule 95-5.04, Promotional Shares, filed 9-27-95;

SD Rule 86-5.05, Insiders Equity, filed 7-11-86;

SD Rule 95-5.24, Impoundment of Proceeds, filed 9-27-95;

SD Rule 95-5.25, Loans and Other Material Affiliated Transactions, filed 9-27-95; and

SD Rule 95-5.26, Debt Securities, filed 9-27-95 were **renumbered** into first version of the New Mexico Administrative Code as 12 NMAC 11.4, Registration and Exemption of Securities, effective 5-1-1999.

That relevant portion of 12 NMAC 11.4; numbered Subpart 8, Registration of Securities (filed 4-19-99) and Subpart 10, Adoption of NASAA Statements of Policy for Registration of Certain Types of Securities (filed 4-19-99) were **renumbered, reformatted, and replaced by** 12.11.9 NMAC, Standards Applicable to Registered Offerings, effective 1-1-2010.