

The background of the slide is a collage of overlapping US one hundred dollar bills. The bills are oriented in various directions, creating a sense of movement and abundance. The portrait of Benjamin Franklin is prominent on several bills, and the text "ONE HUNDRED DOLLARS" and "FEDERAL RESERVE NOTE" is visible. The serial number "DF 20493661 B" is repeated on multiple bills.

Business Law and Bankruptcy

Class 11



Sources of Corporate Funding

- Operating Funds: (use company profits to finance the company's operations)
 - Pro:
 - Does not lead the company into debt
 - Cons:
 - Company has to have sufficient profits to meet operating expenses and salaries
 - Cannot use that money for dividends
- Take out loans from banks
 - Pro:
 - Relatively painless way to raise cash and postpone the repayment
 - Cons:
 - Requires good credit to get a significant loan
 - Too much debt on the corporate balance sheet is not good (the corporate profits might be swallowed up trying to pay off the loans)



Sources of Corporate Funding (cont.)

- Issue shares of the company
 - Pros:
 - Can raise a lot of money without getting the company into debt
 - Cons:
 - Must comply with strict SEC Regulations
 - Dilutes the value of the shares held by the current shareholders
- Issue corporate bonds (loans to the company by private people)
 - Pro:
 - Can raise a lot of money without diluting the shares
 - Cons:
 - Must comply with strict SEC Regulations
 - Adds to the company debt



The SEC Acts- An Overview

- These laws were passed on 1933 and 1934 in response to the stock market crash of 1929 and the ensuing Great Depression.
- Reasons for the passage:
 - Rampant speculation based on faulty information had led to the stock market “bubble” of the 1920s.
 - The faulty information had come from companies who essentially said anything they wanted to get people to buy their shares, with little oversight.
- Goals of the Securities Laws
 - Assure the accuracy and completeness of information given to the investment public
 - Organize a system by which there should be full disclosure of accounting information to the public
 - Regulate all forums in which securities are exchanged



Going Public - The Offering Process

- The key elements to the SEC rules regarding a company going public are:
 - Disclosure:
 - A full and complete disclosure of all sorts of information relating to the company's finances, business, prospects, etc.
 - Organization:
 - The rules require that the company get its books in order before going public.



Initial Public Offering

- The Prospectus:
 - This is the documents that makes these disclosures, explains how the company is organized, and gives investors the information they need to make their investment decisions.
 - The prospectus must be approved by the SEC before the issuance can take place.
 - A prospectus is NOT an advertisement; it may not try to “condition the market” by bragging too much about the company or making predictions. It must stick to the facts!
 - The one section that can prognosticate a little is the “Management’s Discussion and Analysis” section, but that section must not be misleading.
- The Issuance:
 - Occurs only once the SEC has given its approval
 - The corporation or its bank sets the initial price (at which the company offers it to the public), and the free market will soon set the “true” price of the stock.



QUIZ TIME!



The Securities Markets

- A securities market is the “place” at which exchanges of securities take place. They can be physical or on a computer.
- Securities Exchanges
 - These are very heavily regulated by the SEC and are licensed and approved by the SEC to allow people to exchange securities in their “markets.”
- Major Examples:
 - **New York Stock Exchange (NYSE)**: the biggest one, it has its own very strict requirements for its companies, including large public floats and restrictions on who can make up the companies’ boards of directors.
 - **American Stock Exchange (AMEX)**
 - **National Association of Securities Dealers Automated Quotation (NASDAQ)**: Runs electronically. The NASDAQ’s requirements are less stringent, and so they’re often used by new companies or those that are not so wealthy or established.
 - **Over-the Counter Stock trading**: This is trading done privately without an exchange. (Remember that the SEC requirements for going public do not include becoming listed on an exchange.)



Insider Trading

- **Rule 10b(5)**

- This rule prohibits using any fraud or dishonesty in stock trading.
- It also includes people who use “insider information” to make a trade.
 - “Insider information” means information gained in the capacity as officer or director of the company.

- **Rule 16b**

- The “short swing” rule, which is designed to prevent insider trading.
- This rule says that if any transaction is made by an insider up to 6 months before a major announcement that causes a big price fluctuation in the stock, the insider must give back profits made on that transaction.

- **Remedies:**

- Civil and/or criminal penalties
- Disgorgement of profits made on the insider transaction