

STATEMENT OF POLICY REGARDING CORPORATE SECURITIES DEFINITIONS

Adopted April 27, 1997; Amended September 28, 1999, March 31, 2008 and May 6, 2018

I. INTRODUCTION

This Statement of Policy Regarding Definitions applies to definitions used in the following NASAA Statements of Policy:

Statement of Policy Regarding the Impoundment of Proceeds
Statement of Policy Regarding Loans and Other Material Transactions
Statement of Policy Regarding Options and Warrants
Statement of Policy Regarding Preferred Stock
Statement of Policy Regarding Promoters' Equity Investment
Statement of Policy Regarding Promotional Shares
Statement of Policy Regarding Specificity in Use of Proceeds
Statement of Policy Regarding Underwriting and Selling Expenses, Underwriter's Warrants,
and Selling Security Holders
Statement of Policy Regarding Unsound Financial Condition
Statement of Policy Regarding Voting Rights

II. The following words and terms have the meanings set forth below.

- A. Adjusted Net Earnings means the issuer's Net Earnings after charges for interest and dividends, adjusted on a pro forma basis to reflect:
1. The elimination of any required charges for debt, debt securities, or preferred stock that are to be redeemed or retired from the proceeds of the public offering of preferred stock;
 2. The effect of any acquisitions or capital expenditures that the issuer made after its last fiscal year, or that it proposes or is required to make during the current fiscal year, which materially affect the issuer's Net Earnings;
 3. The effect of any dividends or charges on debt, debt securities or preferred stock issued after the issuer's last fiscal year;
 4. The effect of any dividends or charges on debt, debt securities or preferred stock issued during the issuer's last fiscal year, but outstanding for only a portion of the year. Such dividends or charges must be calculated as if the debt, debt securities or preferred stock had been outstanding for the entire fiscal year; and
 5. The effect of any other material changes to an issuer's future Net Earnings.
- B. Administrator means the agency that regulates the securities industry in the applicable jurisdiction.

- C. Affiliate means a Person who, directly or indirectly, Controls, is Controlled by, or is under common Control with a Person as defined in this statement of policy.
- D. Aggregate Revenues means the total revenues, excluding interest and extraordinary items a Person has received during:
1. The last three consecutive fiscal years immediately before the public offering, and
 2. The period during the current fiscal year for which interim period financial information is included in the prospectus.
- E. Associate, when used to indicate a relationship with a Person, includes:
1. 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 (5%) or more of any class of Equity Securities;
 2. 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
 3. A Person's spouse and relatives, by blood or by marriage, if that Person is a Promoter of the issuer, its subsidiaries, its Affiliates, or its parent.
- F. Average Promotional Price means the average per share price paid for Promotional Shares and other shares issued prior to the public offering that 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.
- G. Cash Analysis is the issuer's "Net Cash Provided By Operating Activities" as reflected on the Statement of Cash Flows and determined in accordance with generally accepted accounting principles. If the issuer will use the proceeds of the public offering to redeem or retire debt securities, the issuer must adjust, on a pro forma basis, for the elimination of the related interest charges, net of applicable income taxes.
- H. Control means 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. A presumption of Control exists for any Person who:
1. Is a director, general partner, member, manager, or officer exercising executive responsibility (or has similar status or functions);
 2. Has the right to vote twenty percent (20%) or more of a class of voting securities;
or

3. In the case of a partnership or limited liability company, has contributed or has the right to receive upon dissolution twenty percent (20%) or more of the capital.
- I. Disclosure Document means a prospectus, information statement, offering circular or other offering document.
- J. Equity Securities include shares of common stock or similar securities, convertible securities, and warrants, and options or rights that may be converted into or exercised to purchase shares of common stock or similar securities.
- K. Escrow Agent means:
1. A financial institution whose principal place of business and domicile is in the United States or Canada and that is not affiliated with the issuer, its Promoters, or Associates. A financial institution may act as an Escrow Agent even if the issuer, its Promoters or Associates are its customers.
 2. An attorney or certified public accountant, provided that the attorney or certified public accountant:
 - i. Is not affiliated with the issuer, its Promoters, or their Associates;
 - ii. Is licensed to do business in the state in which the attorney or certified public accountant practices; and
 - iii. Can demonstrate adequate insurance or can provide a fidelity bond.
- L. Impoundment Agent means a depository institution as defined in Section 102(5) of the Uniform Securities Act of 2002 that is domiciled and whose principal place of business is located in the United States or Canada.
- M. Independent Director means a member of an issuer's board of directors who:
1. Does not receive, other than in the director's capacity as a member of the board of directors or a board committee, any consulting, advisory or other compensatory fee from the issuer, its subsidiaries, or their Affiliates or Associates;
 2. Has not received any compensation or fees from the issuer, its subsidiaries, Affiliates, or Associates within the last two years other than in the director's capacity as a member of the board of directors or a board committee;
 3. Other than serving as a director of the issuer, is not a Promoter as defined below; and

4. Does not have a material business or professional relationship with the issuer or any of its Affiliates or Associates. For purposes of determining whether or not a business or professional relationship is material, the gross revenue that the Independent Director derives from the issuer, its Affiliates and Associates is deemed material if it exceeds 5% 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.

- N. Lock-In Agreement means an agreement entered into between an issuer and a Person as a condition of registration in which the Person agrees not to dispose of or otherwise transfer Equity Securities the Person received from the issuer or that the issuer granted to the Person.

- O. Net Earnings means the issuer's after-tax earnings, excluding extraordinary and nonrecurring items, determined in accordance with generally accepted accounting principles.

- P. Person means an individual, corporation, business trust, estate, trust, partnership, limited liability company, limited liability partnership, association, joint venture, government; governmental subdivision, agency, or instrumentality; public corporation; or any legal or commercial entity.

- Q. Promoter:
 1. Includes a Person who:
 - i. 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;
 - ii. Directly or indirectly, receives, as consideration for property or for services rendered, five percent (5%) or more of any class of the issuer's Equity Securities or five percent (5%) or more of the proceeds from the sale of any class of the issuer's Equity Securities;
 - iii. Is an officer or director for the issuer;
 - iv. Legally or beneficially owns, directly or indirectly, five percent (5%) or more of any class of the issuer's Equity Securities; or
 - v. Is an Affiliate or an Associate of a Person specified in paragraphs i through iv, above.

2. Does not include:
 - i. A Person who receives securities or proceeds solely as underwriting compensation unless that Person otherwise comes within the term;
 - ii. An Unaffiliated Institutional Investor, who purchased the issuer's Equity Securities more than one year prior to the filing date of the issuer's registration statement; or
 - iii. At the Administrator's discretion, an Unaffiliated Institutional investor, who purchased the issuer's Equity Securities on an arm's-length basis within one year prior to the filing date of the issuer's registration statement.

- R. Promoters' Equity Investment means the total of cash and assets Promoters contributed to the issuer, provided that the Administrator accepts the value of the tangible or intangible assets.

- S. Promotional Or Development Stage Company means an issuer:
 1. That is not listed, or authorized for listing, on the New York Stock Exchange, the American Stock Exchange, the NASDAQ Global Market, or a securities exchange that the Securities and Exchange Commission determines under Section 18(b)(1) of the Securities Act of 1933 has substantially similar listing standards;
 2. That has had annual Net Earnings for each of the last two (2) consecutive fiscal years before the public offering that have been less than five percent (5%) of the aggregate public offering; or
 3. That has had average, annual Net Earnings for the last five (5) fiscal years before the public offering that have been less than five percent (5%) of the aggregate public offering.

- T. Promotional Shares mean Equity Securities that:
 1. A Promotional Or Development Stage Company has issued within five (5) years before the filing of the registration statement or will issue to its Promoters for cash or other consideration, including services rendered, patents, copyrights, and other intangibles; or
 2. An issuer that is not a Promotional Or Development Stage Company has issued within three (3) years before the filing of the registration statement or will issue to Promoters for cash or other consideration, including services rendered, patents, copyrights and other intangibles.

- U. Public Offering Price means the per share price at which a Promotional Or Development Stage Company proposes to offer Equity Securities to the public.
- V. Unaffiliated Institutional Investor means the following investors if not Affiliated with the issuer:
1. An institutional investor as defined in Section 102(11) of the Uniform Securities Act of 2002; and
 2. A business development Company as defined in Section 2(a)(48) of the Investment Company Act of 1940.
- W. Underwriter means any Person that has agreed with the issuer or with another Person on whose behalf a distribution is to be made:
1. To purchase securities for distribution;
 2. To distribute securities on behalf of the issuer or other Person; or
 3. To manage or supervise a distribution of securities on behalf of the issuer or other Person.
- X. Underwriting and Selling Expenses means the expenses directly or indirectly incurred in the sale of registered securities, including, but not limited to the following:
1. Commissions to Underwriters or broker dealers;
 2. Non-accountable fees or expenses to be paid to Underwriters or broker-dealers;
 3. The value of Underwriter's warrants;
 4. Rights of first refusal, to be valued at 1% 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, to be valued at the lesser of actual cost or 1% of the public offering if the fees are payable within one year of the offering;
 6. Fees payable to an underwriter under financial consulting or financial advisory agreements, or any other similar type of agreement, however designated, which shall be valued at actual cost, excluding financial consulting or financial advisory agreements that are entered into at least twelve months before the issuer files a registration statement with the Securities and Exchange Commission;

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 that the Underwriter designated;
9. Other underwriting expenses incurred in connection with the public offering of securities that the Administrator determines;
10. Auditor's and accountant's fees;
11. Legal fees;
12. The cost of printing Disclosure Documents required to comply with securities laws and regulations;
13. Charges of transfer agents, registrars, indenture trustees, escrow holders, depositories, engineers, appraisers, and other experts;
14. The cost of authorizing and preparing the securities, including issue taxes and stamps;
15. Expenses incurred in connection with bridge financing in the twelve month period preceding a public offering of securities, including, but not limited to:
 - i. Direct expenses attributable to the financing, including interest charges, and underwriting expenses;
 - ii. The value of warrants and options; and
 - iii. Expenses attributable to the issuance of the securities that are not options, warrants, or convertible securities valued by the following formula:

$$\frac{(\text{Public Offering Price per share} - \text{Cost per share}) \times \text{Number of Securities Issued} \times 100}{\text{Aggregate Public Offering Proceeds}}$$
; and

16. Other cash expenses incurred in connection with the public offering of securities as determined by the Administrator.

Y. Unsound Financial Condition means:

1. The auditor's report accompanying the issuer's financial statements contains an explanatory paragraph or qualification regarding the issuer's ability to continue as a going concern; or
2. One or more of the following applies:

- i. The issuer has an accumulated deficit;
- ii. The issuer has negative shareholder equity;
- iii. The issuer is not able to satisfy current obligations as they come due; or
- iv. The issuer has negative cash flow.

Drafters' Commentary: Section II.T.1 is consistent with section 305(f) of the Uniform Securities Act of 2002 (USA), which allows a state to require as a condition of registration the escrow of shares issued within the previous five years for consideration that is substantially less than the public offering price. A state that has a statutory 'look-back' that differs from the USA should modify the look-back provision of Section II.T to comply with its statute.