



SEC Proposal Will Permit General Solicitation and General Advertising in Rule 506 Offerings

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On August 29, 2012, the Securities and Exchange Commission (SEC) published Release No. 33-9354, which sets forth proposed amendments to Rule 506 of Regulation D under the Securities Act of 1933 (Securities Act). The amendments are required under Section 201(a) of the Jumpstart Our Business Startups Act, or JOBS Act, which was adopted earlier this year. Under the newly proposed rules, the prohibition against general solicitation and general advertising will not apply to offers and sales of securities made pursuant to Rule 506.

Proposed Rule 506(c)

To implement the change, the SEC has proposed adding new Rule 506(c) which would permit the use of general solicitation to offer and sell securities under Rule 506 so long as:

- the issuer takes reasonable steps to verify that the purchasers of the securities are accredited investors;
- all purchasers of securities must be accredited investors, either because they come within one of the enumerated categories of persons that qualify as accredited investors or the issuer reasonably believes that they do, at the time of the sale of securities; and
- all terms and conditions of Rules 501, 502(a) and 502(d) are satisfied.

Form D will also be revised to include a check box where issuers will indicate whether they are relying on the exemption under Rule 506(c).

With respect to what constitutes “reasonable steps” to verify that purchasers of the securities are accredited investors, the SEC has proposed an objective determination based on the particular facts and circumstances of each transaction. Although the SEC did not issue a checklist or mandate that issuers undertake a specific verification method to confirm status, it did provide a number of factors which may be considered, including:

- the nature of the purchaser and the type of accredited investor that the purchaser claims to be;
- the amount and type of information that the issuer has about the purchaser; and
- the nature of the offering, such as the manner of solicitation and the terms of the offering.

The SEC suggested how various factors, when taken together, could increase or decrease the amount of verification that an issuer must complete. For example, a solicitation of the general public through a website or social media will require more steps to verify accredited investor status than a solicitation of purchasers by a registered broker-dealer. In a solicitation of the general public, having the investor check a box on a questionnaire or sign a form will not constitute “reasonable steps to verify” accredited investor status, unless the issuer has additional verifying information. The SEC indicated that

additional verification steps could include the use of third party verification services that provide reliable evidence that a purchaser qualifies as an accredited investor.

The nature and terms of the offering may also be used as factors to verify accredited investor status. These factors include the minimum investment amount of the offering, which if high enough, could be relied upon as an additional factor in verifying whether a purchaser is accredited. The SEC emphasized that the issuer should maintain adequate records indicating the steps taken to verify whether purchasers are accredited investors since any issuer claiming an exemption from the registration requirements of the Securities Act has the burden of showing that it is entitled to such an exemption. If an issuer takes reasonable steps to verify accredited investor status and reasonably believes that a purchaser is an accredited investor, then the issuer will not lose the ability to rely on the exemption under Rule 506(c) even if such purchaser turns out not to be an accredited investor.

Existing Rules Unchanged

The SEC has preserved the ability of issuers to conduct private offerings under Rule 506 without the use of general solicitation. Under Rule 506(b), issuers must reasonably believe that purchasers are accredited investors. The stricter requirement of taking

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reasonable steps to verify that purchasers are accredited investors does not apply to offerings under rule 506(b). In addition, the SEC confirmed that concurrent Regulation S and Regulation D offerings to overseas and U.S. investors, respectively, will not be integrated if issuers engage in general solicitation in the U.S.

What's Next

The SEC is accepting public comments on the proposed rules until October 5,

2012 with final rules expected shortly thereafter.

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