

# BURR ALERT

## New Rules Would Facilitate Securities Sales

July 15, 2013

On July 10, 2013, the Securities and Exchange Commission (SEC) promulgated long-awaited rules which will allow and govern how business owners and entrepreneurs may use media and advertising to reach potential investors. The rules implement a requirement in the 2012 JOBS Act to lift the ban on “general solicitation” under current Rule 506 of Regulation D, the most frequently utilized framework in qualifying a securities offering as exempt from registration with the SEC. In essence, those offering securities would be permitted under federal law to use internet communications, aggregation sites, and general advertisements to solicit investments so long as the actual purchaser of the securities is an "accredited investor" (see further information below) and the offeror undertakes reasonable measures to verify that purchasers qualify as accredited investors. The rules are subject to a 60-day comment period, and the earliest such will become effective is September 2013.

The background on the significant, company-friendly change of law, and the features of the proposed SEC release, are as follows:

**Current Law and JOBS Act:** Companies seeking to raise capital through the sale of securities must either register the securities offering with the SEC or rely on an exemption from registration. Rule 506 of Regulation D is the most widely-used exemption from registration as neither the number of investors nor the amount of capital raised thereunder is limited. In this exemption as in others, issuers of securities are prohibited from engaging in general solicitation or general advertising, including advertisements on the internet or in other publications. In April 2012, Congress passed the Jumpstart Our Business Startups Act (JOBS Act). Section 201(a)(1) of the JOBS Act directs the SEC to remove the prohibition on general solicitation or general advertising for securities offerings relying on Rule 506 provided that sales are limited to accredited investors and an issuer takes reasonable steps to verify that all purchasers of the securities are accredited investors. By requiring the SEC to remove this restriction, Congress sought to make it easier for a company to find investors and raise capital.

**Actions by the SEC and the July 2013 Releases.** Last August, the SEC offered proposed rules, which received numerous comments focus providing greater clarification on what types of verification are reasonable as well as investor protections for investors in connection with

removing the general solicitation ban. The final rules amend Rule 506 and permit issuers to use general solicitation and general advertising provided that:

- >> All purchasers of the securities qualify as accredited investors (see below) under Rule 501 of Regulation D or the issuer reasonably believes that the investors fall within one of the categories at the time of the sale of the securities.
- >> A person qualifies as an accredited investor if he or she has either: (i) an individual net worth or joint net worth with a spouse that exceeds \$1 million at the time of the purchase, excluding the value (and any related indebtedness) of a primary residence, or (ii) an individual annual income that exceeded \$200,000 in each of the two most recent years or a joint annual income with a spouse exceeding \$300,000 for those years, and a reasonable expectation of the same income level in the current year.
- >> The issuer takes reasonable steps to verify that the investors are accredited investors, with which respect to individual investors may include reviewing copies of any IRS form that reports the income of the purchaser, obtaining a written representation that the purchaser will likely continue to earn the necessary income in the current year and/or receiving a written confirmation from a registered broker-dealer, SEC-registered investment adviser, licensed attorney, or certified public accountant.

**Rule 144A (Institutional Investors).** The JOBS Act also directs the SEC to amend Rule 144A under the Securities Act, which is an exemption from registration that applies to the resale of securities to larger institutional investors known as qualified institutional buyers (QIBs). Under the new rules, Rule 144A is amended so that resale securities offerings can be made to QIBs as well as investors who are not QIBs so long as the securities are sold only to persons whom the seller reasonably believes are QIBs --with similar verification standards as discussed per above with respect to accredited investors.

**Form D.** The final rule amends Form D, which is the notice that issuers must file with the SEC when they sell securities under Regulation D. The revised form adds a separate box for issuers to check if they are claiming the new Rule 506 exemption permitting general solicitation or general advertising.

**Other Changes to Regulation D Under Separate Rules.** In a separate release to that discussed above, the SEC offered a number of proposed amendments to Regulation D, Form D and Rule 156, as intended to enhance the SEC's ability to evaluate the development of market practices in Rule 506 offerings under the new rules. Specifically, the SEC would require written general solicitation materials used in Rule 506(c) offerings to include certain legends and other disclosures; require

the submission, on a temporary basis, of written general solicitation materials used in Rule 506(c) offerings to the SEC; and disqualify an issuer from relying on Rule 506 for one year for future offerings if the issuer, or any predecessor or affiliate of the issuer, did not comply, within the last five years, with Form D filing requirements in a Rule 506 offering.

**Effectiveness.** The rule amendments become effective 60 days after publication in the Federal Register.

**For more information on this significant development in accessing potential investors, contact:**

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