was the subject of a refusal order, stop order, or order suspending the Regulation A exemption, or is, at the time of such sale, the subject of an investigation or proceeding to determine whether a stop order or suspension order should be issued; or

(viii) Is subject to a United States Postal Service false representation order entered within five years before such sale, or is, at the time of such sale, subject to a temporary restraining order or preliminary injunction with respect to conduct alleged by the United States Postal Service to constitute a scheme or device for obtaining money or property through the mail by means of false representations.

(2) Paragraph (d)(1) of this section shall not apply:

(i) With respect to any conviction, order, judgment, decree, suspension, expulsion or bar that occurred or was issued before September 23, 2013;

(ii) Upon a showing of good cause and without prejudice to any other action by the Commission, if the Commission determines that it is not necessary under the circumstances that an exemption be denied;

(iii) If, before the relevant sale, the court or regulatory authority that entered the relevant order, judgment or decree advises in writing (whether contained in the relevant judgment, order or decree or separately to the Commission or its staff) that disqualification under paragraph (d)(1) of this section should not arise as a consequence of such order, judgment or decree; or

(iv) If the issuer establishes that it did not know and, in the exercise of reasonable care, could not have known that a disqualification existed under paragraph (d)(1) of this section.

Instruction to paragraph (d)(2)(iv). An issuer will not be able to establish that it has exercised reasonable care unless it has made, in light of the circumstances, factual inquiry into whether any disqualifications exist. The nature and scope of the factual inquiry will vary based on the facts and circumstances concerning, among other things, the issuer and the other offering participants.

(3) For purposes of paragraph (d)(1) of this section, events relating to any affiliated issuer that occurred before the affiliation arose will be not considered disqualifying if the affiliated entity is not:

(i) In control of the issuer; or

(ii) Under common control with the issuer by a third party that was in control of the affiliated entity at the time of such events.

(e) *Disclosure of prior ''bad actor'' events.* The issuer shall furnish to each purchaser, a reasonable time prior to sale, a description in writing of any matters that would have triggered disqualification under paragraph (d)(1) of this section but occurred before September 23, 2013. The failure to furnish such information timely shall not prevent an issuer from relying on this section if the issuer establishes that it did not know and, in the exercise of reasonable care, could not have known of the existence of the undisclosed matter or matters.

Instruction to paragraph (e). An issuer will not be able to establish that it has exercised reasonable care unless it has made, in light of the circumstances, factual inquiry into whether any disqualifications exist. The nature and scope of the factual inquiry will vary based on the facts and circumstances concerning, among other things, the issuer and the other offering participants.

PART 239—FORMS PRESCRIBED UNDER THE SECURITIES ACT OF 1933

■ 10. The authority citation for part 239 continues to read, in part, as follows:

Authority: 15 U.S.C. 77f, 77g, 77h, 77j, 77s, 77z–2, 77z–3, 77sss, 78c, 78*l*, 78m, 78n, 78*o*(d), 78*o*–7 note, 78u–5, 78w(a), 78*ll*, 78mm, 80a–2(a), 80a–3, 80a–8, 80a–9, 80a–10, 80a–13, 80a–24, 80a–26, 80a–29, 80a–30, and 80a–37, unless otherwise noted.

* * * * *

■ 11. Amend Form D (referenced in § 239.500) by revising the third indented paragraph under the heading ''Terms of Submission'' in the ''Signature and Submission'' section following Item 16 to read as follows:

Certifying that, if the issuer is claiming a Regulation D exemption for the offering, the issuer is not disqualified from relying on Regulation D for one of the reasons stated in Rule 505(b)(2)(iii) or Rule 506(d).

Note: The text of Form D does not, and the amendments will not, appear in the Code of Federal Regulations.

By the Commission.

Dated: July 10, 2013.

Elizabeth M. Murphy,

Secretary.

[FR Doc. 2013–16983 Filed 7–23–13; 8:45 am]

BILLING CODE 8010–01–P

SECURITIES AND EXCHANGE COMMISSION

17 CFR Parts 230, 239 and 242

[Release No. 33–9415; No. 34–69959; No. IA–3624; File No. S7–07–12]

RIN 3235–AL34

Eliminating the Prohibition Against General Solicitation and General Advertising in Rule 506 and Rule 144A Offerings

AGENCY: Securities and Exchange Commission.

ACTION: Final rules.

SUMMARY: We are adopting amendments to Rule 506 of Regulation D and Rule 144A under the Securities Act of 1933 to implement Section 201(a) of the Jumpstart Our Business Startups Act. The amendment to Rule 506 permits an issuer to engage in general solicitation or general advertising in offering and selling securities pursuant to Rule 506, provided that all purchasers of the securities are accredited investors and the issuer takes reasonable steps to verify that such purchasers are accredited investors. The amendment to Rule 506 also includes a non-exclusive list of methods that issuers may use to satisfy the verification requirement for purchasers who are natural persons. The amendment to Rule 144A provides that securities may be offered pursuant to Rule 144A to persons other than qualified institutional buyers, provided that the securities are sold only to persons that the seller and any person acting on behalf of the seller reasonably believe are qualified institutional buyers. We are also revising Form D to require issuers to indicate whether they are relying on the provision that permits general solicitation or general advertising in a Rule 506 offering.

Also today, in a separate release, to implement Section 926 of the Dodd-Frank Wall Street Reform and Consumer Protection Act, we are adopting amendments to Rule 506 to disqualify issuers and other market participants from relying on Rule 506 if ''felons and other 'bad actors' '' are participating in the Rule 506 offering. We are also today, in a separate release, publishing for comment a number of proposed amendments to Regulation D, Form D and Rule 156 under the Securities Act that are intended to enhance the Commission's ability to evaluate the development of market practices in Rule 506 offerings and address certain comments made in connection with implementing Section 201(a)(1) of the Jumpstart Our Business Startups Act.

DATES: The final rule and form amendments are effective on September 23, 2013.

FOR FURTHER INFORMATION CONTACT: Charles Kwon, Special Counsel, or Ted Yu, Senior Special Counsel, Office of Chief Counsel, Division of Corporation Finance, at (202) 551–3500, or, with respect to private funds, Holly Hunter-Ceci, Senior Counsel, Chief Counsel's Office, or Alpa Patel, Senior Counsel, Investment Adviser Regulation Office, Division of Investment Management, at (202) 551–6825 or (202) 551–6787, Securities and Exchange Commission, 100 F Street NE., Washington, DC 20549.

SUPPLEMENTARY INFORMATION: We are adopting amendments to Rule 144A,[1] Form D,[2] and Rules 500,[3] 501,[4] 502[5] and 506[6] of Regulation D[7] under the Securities Act of 1933,[8] and to Rules 101,[9] 102[10] and 104[11] of Regulation M[12] under the Securities Exchange Act of 1934.[13]

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I. Introduction

On August 29, 2012, we proposed rule and form amendments[14] to implement Section 201(a) of the Jumpstart Our Business Startups Act (the ''JOBS Act'').[15] Section 201(a)(1) of the JOBS Act directs the Commission, not later than 90 days after the date of enactment, to amend Rule 506 of Regulation D[16] under the Securities Act of 1933 (the ''Securities Act'') to permit general solicitation or general advertising in offerings made under Rule 506, provided that all purchasers of the securities are accredited investors.[17] Section 201(a)(1) also states that ''[s]uch rules shall require the issuer to take reasonable steps to verify that purchasers of the securities are accredited investors, using such methods as determined by the Commission.'' Section 201(a)(2) of the JOBS Act directs the Commission, not later than 90 days after the date of enactment, to revise Rule 144A(d)(1) under the Securities Act[18] to permit offers of securities pursuant to Rule 144A to persons other than qualified institutional buyers (''QIBs''),[19] including by means of general solicitation or general advertising, provided that the securities are sold only to persons that the seller and any person acting on behalf of the seller reasonably believe are QIBs.

The Commission originally adopted Rule 506 as a non-exclusive safe harbor under Section 4(a)(2) (formerly Section 4(2)) of the Securities Act,[20] which exempts transactions by an issuer ''not involving any public offering'' from the registration requirements of Section 5 of the Securities Act.[21] Under existing Rule 506, an issuer may sell securities,

[1] 17 CFR 230.144A.
[2] 17 CFR 239.500.
[3] 17 CFR 230.500.
[4] 17 CFR 230.501.
[5] 17 CFR 230.502.
[6] 17 CFR 230.506.
[7] 17 CFR 230.500 through 230.508.
[8] 15 U.S.C. 77a *et seq.*
[9] 17 CFR 242.101.
[10] 17 CFR 242.102.
[11] 17 CFR 242.104.
[12] 17 CFR 242.100 through 242.105.
[13] 15 U.S.C. 78a *et seq.*

[14] *See Eliminating the Prohibition Against General Solicitation and General Advertising in Rule 506 and Rule 144A Offerings,* Release No. 33–9354 (Aug. 29, 2012) [77 FR 54464 (Sept. 5, 2012)] (the ''Proposing Release'').

[15] Public Law 112–106, sec. 201(a), 126 Stat. 306, 313 (Apr. 5, 2012).

[16] The Commission adopted Regulation D in 1982 as a result of the Commission's evaluation of the impact of its rules on the ability of small businesses to raise capital. *See Revision of Certain Exemptions From Registration for Transactions Involving Limited Offers and Sales,* Release No. 33–6389 (Mar. 8, 1982) [47 FR 11251 (Mar. 16, 1982)]. Over the years, the Commission has revised various provisions of Regulation D in order to address, among other things, specific concerns relating to facilitating capital-raising as well as abuses that have arisen under Regulation D. *See, e.g., Additional Small Business Initiatives,* Release No. 33–6996 (Apr. 28, 1993) [58 FR 26509 (May 4, 1993)] and *Revision of Rule 504 of Regulation D, the ''Seed Capital'' Exemption,* Release No. 33–7644 (Feb. 25, 1999) [64 FR 11090 (Mar. 8, 1999)].

[17] The definition of the term ''accredited investor'' that is applicable to Rule 506 is set forth in Rule 501(a) of Regulation D [17 CFR 230.501(a)] and includes any person who comes within one of the definition's enumerated categories of persons, or whom the issuer ''reasonably believes'' comes within any of the enumerated categories, at the time of the sale of the securities to that person. For natural persons, Rule 502(a) defines an accredited investor as a person: (1) Whose individual net worth, or joint net worth with that person's spouse, exceeds $1 million, excluding the value of the person's primary residence (the ''net worth test''); or (2) who had an individual income in excess of $200,000 in each of the two most recent years, or joint income with that person's spouse in excess of $300,000 in each of those years, and has a reasonable expectation of reaching the same income level in the current year (the ''income test'').

Although the Dodd-Frank Act did not change the amount of the $1 million net worth test, it did change how that amount is calculated—by excluding the value of a person's primary residence. This change took effect upon the enactment of the Dodd-Frank Act. In December 2011, we amended Rule 501 to incorporate this change into the definition of accredited investor. *See Net Worth Standard for Accredited Investors,* Release No. 33–9287 (Dec. 21, 2011) [76 FR 81793 (Dec. 29, 2011)].

[18] 17 CFR 230.144A(d)(1).

[19] The term ''qualified institutional buyer'' is defined in Rule 144A(a)(1) [17 CFR 230.144A(a)(1)] and includes specified institutions that, in the aggregate, own and invest on a discretionary basis at least $100 million in securities of issuers that are not affiliated with such institutions. Banks and other specified financial institutions must also have a net worth of at least $25 million. A registered broker-dealer qualifies as a QIB if it, in the aggregate, owns and invests on a discretionary basis at least $10 million in securities of issuers that are not affiliated with the broker-dealer.

[20] 15 U.S.C. 77d(a)(2).

[21] 15 U.S.C. 77e.

without any limitation on the offering amount, to an unlimited number of ''accredited investors,'' as defined in Rule 501(a) of Regulation D, and to no more than 35 non-accredited investors who meet certain ''sophistication'' requirements.[22] The availability of Rule 506 is subject to a number of requirements[23] and is currently conditioned on the issuer, or any person acting on its behalf, not offering or selling securities through any form of ''general solicitation or general advertising.''[24] Although the terms ''general solicitation'' and ''general advertising'' are not defined in Regulation D, Rule 502(c) does provide examples of general solicitation and general advertising, including advertisements published in newspapers and magazines, communications broadcast over television and radio, and seminars where attendees have been invited by general solicitation or general advertising.[25] By interpretation, the Commission has confirmed that other uses of publicly available media, such as unrestricted Web sites, also constitute general solicitation and general advertising.[26] In this release, we refer to both general solicitation and general advertising as ''general solicitation.''

Rule 144A is a non-exclusive safe harbor exemption from the registration requirements of the Securities Act for resales of certain ''restricted securities''[27] to QIBs. Resales to QIBs in accordance with the conditions of Rule 144A[28] are exempt from registration pursuant to Section 4(a)(1) (formerly Section 4(1)) of the Securities Act,[29] which exempts transactions by any person ''other than an issuer, underwriter, or dealer.'' Although Rule 144A does not include an express prohibition against general solicitation, offers of securities under Rule 144A currently must be limited to QIBs, which has the same practical effect. By its terms, Rule 144A is available solely for resale transactions; however, since its adoption by the Commission in 1990,[30] market participants have used Rule 144A to facilitate capital-raising by issuers.[31] The term ''Rule 144A offering'' in this release refers to a primary offering of securities by an issuer to one or more financial intermediaries—commonly known as the ''initial purchasers''—in a transaction that is exempt from registration pursuant to Section 4(a)(2) or Regulation S under the Securities Act,[32] followed by the resale of those securities by the initial purchasers to QIBs in reliance on Rule 144A.

Rule 506 offerings and Rule 144A offerings are widely used by U.S. and non-U.S. issuers to raise capital. In 2012, the estimated amount of capital (including both equity and debt) reported as being raised in Rule 506 offerings and non-asset-backed securities (''non-ABS'') Rule 144A offerings by operating companies was $173 billion and $636 billion, respectively, and by pooled investment funds, such as venture capital funds, private equity funds and hedge funds, was $725 billion and $4 billion, respectively, compared to $1.2 trillion raised in registered offerings.[33] In 2011, the estimated amount of capital (including both equity and debt) reported as being raised in Rule 506 offerings and non-ABS Rule 144A offerings by operating companies was $71 billion and $438 billion, respectively, and by pooled investment funds was $778 billion and $4 billion, respectively, compared to $985 billion raised in registered offerings.[34] These data points underscore the importance of the Rule 506 and Rule 144A exemptions for issuers seeking access to the U.S. capital markets.

To implement Section 201(a) of the JOBS Act, we proposed amending Rule 506 to add new paragraph (c), under which the prohibition against general solicitation contained in Rule 502(c) would not apply, provided that all purchasers of the securities are accredited investors and the issuer takes reasonable steps to verify that such purchasers are accredited investors. In addition, we proposed amending Form D, which is a notice required to be filed with the Commission by each issuer

[22] Under Rule 506(b)(2)(ii) [17 CFR 230.506(b)(2)(ii)], each purchaser in a Rule 506 offering who is not an accredited investor must possess, or the issuer must reasonably believe immediately before the sale of securities that such purchaser possesses, either alone or with his or her purchaser representative, ''such knowledge and experience in financial and business matters that he [or she] is capable of evaluating the merits and risks of the prospective investment.''

[23] Offerings under Rule 506 are subject to all the terms and conditions of Rules 501 and 502. If securities are sold to any non-accredited investors, specified information requirements apply. *See* Rule 502(b) [17 CFR 230.502(b)].

[24] Rule 502(c) of Regulation D [17 CFR 230.502(c)].

[25] *Id.*

[26] *See Use of Electronic Media for Delivery Purposes,* Release No. 33–7233 (Oct. 6, 1995) [60 FR 53458, 53463–64 (Oct. 13, 1995)]; *Use of Electronic Media,* Release No. 33–7856 (Apr. 28, 2000) [65 FR 25843, 25851–52 (May 4, 2000)].

[27] ''Restricted securities'' are defined in Securities Act Rule 144(a)(3) [17 CFR 230.144(a)(3)] to include, in part, ''[s]ecurities acquired directly or indirectly from the issuer, or from an affiliate of the issuer, in a transaction or chain of transactions not involving any public offering.''

[28] In order for a transaction to come within existing Rule 144A, a seller must have a reasonable basis for believing that the offeree or purchaser is a QIB and must take reasonable steps to ensure that the purchaser is aware that the seller may rely on Rule 144A. Further, only securities that were not, when issued, of the same class as securities listed on a U.S. securities exchange or quoted on a U.S. automated interdealer quotation system are eligible for resale under Rule 144A. Also, the seller and a prospective purchaser designated by the seller must have the right to obtain from the issuer, upon request, certain information on the issuer, unless the issuer falls within specified categories as to which this condition does not apply.

[29] 15 U.S.C. 77d(a)(1).

[30] *See Resale of Restricted Securities; Changes to Method of Determining Holding Period of Restricted Securities Under Rules 144 and 145,* Release No. 33–6862 (Apr. 23, 1990) [55 FR 17933 (Apr. 30, 1990)].

[31] While Rule 144A applies to resales of securities of both U.S. and non-U.S. issuers, one of the objectives of Rule 144A was to make primary offerings of non-U.S. issuers' securities available to U.S. institutions in the U.S. market through intermediaries (rather than compelling such investors to go to overseas markets) by making the private offering market in the United States more attractive to non-U.S. issuers. *See Resale of Restricted Securities; Changes to Method of Determining Holding Period of Restricted Securities Under Rules 144 and 145,* Release No. 33–6806 (Oct. 25, 1988) [53 FR 44016 (Nov. 1, 1988)].

[32] Regulation S under the Securities Act [17 CFR 230.901 through 230.905] was adopted in 1990 as a safe harbor from the registration requirements of the Securities Act for any offer or sale of securities made outside the United States. It provides that any ''offer,'' ''offer to sell,'' ''sell,'' ''sale'' or ''offer to buy'' that occurs outside the United States is not subject to the registration requirements of Section 5. Regulation S does not affect the scope or availability of the antifraud or other provisions of the Securities Act to offers and sales made in reliance on Regulation S.

[33] These statistics are based on a review of Form D electronic filings with the Commission—specifically, the ''total amount sold'' as reported in the filings—and data regarding other types of offerings (*e.g.,* public debt offerings and Rule 144A offerings) from Securities Data Corporation's New Issues database (Thomson Financial). *See* Vladimir Ivanov and Scott Bauguess, *Capital Raising in the U.S.: An Analysis of Unregistered Offerings Using the Regulation D Exemption, 2009–2012* (July 2013) (the ''Ivanov/Bauguess Study''), *available at: http://www.sec.gov/divisions/riskfin/whitepapers/dera-unregistered-offerings-reg-d.pdf.* For non-ABS Rule 144A offerings, since the databases we used to obtain the Rule 144A data do not distinguish between operating companies and funds, we classified issuers with SIC codes between 6200 and 6299 as funds, and the rest as operating companies.

The amount of capital raised through offerings under Regulation D may be larger than what is reported in Form D filings because, although the filing of a Form D is a requirement of Rule 503(a) of Regulation D [17 CFR 230.503(a)], it is not a condition to the availability of the exemptions under Regulation D. Further, once a Form D is filed, the issuer is not required to file an amendment to the filing to reflect a change that occurs after the offering terminates or a change that occurs solely with respect to certain information, such as the amount sold in the offering. For example, if the amount sold does not result in an increase in the total offering amount of more than 10% or the offering closes within a year, the filing of an amendment to the initial Form D is not required. Therefore, a Form D filed for a particular offering may not reflect the total amount of securities sold in the offering in reliance on the exemption.

[34] *See id.*

claiming a Regulation D exemption, to add a check box to indicate whether an issuer is claiming an exemption under Rule 506(c). We also proposed an amendment to Rule 144A to provide that securities sold pursuant to Rule 144A may be offered to persons other than QIBs, including by means of general solicitation, provided that the securities are sold only to persons that the seller and any person acting on behalf of the seller reasonably believe are QIBs.

The comment period for the proposed rule and form amendments closed on October 5, 2012. We received over 225 comment letters on the Proposing Release, including from professional and trade associations, investor organizations, law firms, investment companies and investment advisers, members of Congress, the Commission's Investor Advisory Committee,[35] state securities regulators, issuers, individuals and other interested parties. Most of the comment letters focused on the proposed amendments to Rule 506. As discussed below, commenters were sharply divided in their views on the proposed amendments to Rule 506, whereas commenters generally supported the proposed amendments to Rule 144A and Form D.

We have reviewed and considered all of the comments that we received on the proposed rule and form amendments and on Section 201(a) of the JOBS Act.[36] We are adopting new paragraph (c) to Rule 506 as proposed, with one modification, and the amendments to Form D and to Rule 144A as proposed. We are also adopting the technical and conforming rule amendments as proposed. We discuss these amendments in detail below.

We acknowledge the concerns of some commenters that the elimination of the prohibition against general solicitation for a subset of Rule 506 offerings may affect the behavior of issuers and other market participants in ways they believe could compromise investor protection.[37] Preserving the integrity of the Rule 506(c) market and minimizing the incidence of fraud are critical objectives for the Commission in implementing Section 201(a) of the JOBS Act. We are adopting today the bad actor disqualification for Rule 506 offerings mandated by the Dodd-Frank Act, which may address some of those concerns.[38] We are also issuing a proposing release to amend Regulation D and Form D to enhance the Commission's ability to analyze the Rule 506 market and to amend Rule 156 under the Securities Act to provide guidance to private funds on the application of the antifraud provisions of the federal securities laws to their sales literature.[39] Upon the effectiveness of Rule 506(c), the Commission staff will monitor developments in the market for Rule 506(c) offerings so as to be able to undertake a review of market practices in Rule 506(c) offerings, including the steps taken by issuers and other market participants to verify that the purchasers of the offered securities are accredited investors, as well as the impact of the amendments to Rule 506 on capital formation.

II. Final Amendments to Rule 506 and Form D

A. Eliminating the Prohibition Against General Solicitation

Section 4(a)(2) of the Securities Act exempts transactions by an issuer ''not involving any public offering.'' An issuer relying on Section 4(a)(2) is restricted in its ability to make public communications to attract investors for its offering because public advertising is incompatible with a claim of exemption under Section 4(a)(2).[40] As noted above, Rule 506 currently conditions the availability of the safe harbor under Section 4(a)(2) on the issuer, or any person acting on its behalf, not offering or selling securities through any form of general solicitation.[41] Section 201(a)(1) of the JOBS Act directs the Commission to amend Rule 506 to provide that the prohibition against general solicitation contained in Rule 502(c) shall not apply to offers and sales of securities made pursuant to Rule 506, as so amended, provided that all purchasers of the securities are accredited investors and the issuer takes reasonable steps to verify their status as accredited investors.

This mandate affects only Rule 506, and not Section 4(a)(2) offerings in general,[42] which means that even after the effective date of Rule 506(c), an issuer relying on Section 4(a)(2) outside of the Rule 506(c) exemption will be restricted in its ability to make public communications to solicit investors for its offering because public advertising will continue to be incompatible with a claim of exemption under Section 4(a)(2). We are amending Rule 500(c) of Regulation D accordingly to make this clear.[43] Congress' directive in Section 201(a)(1) of the JOBS Act, and not Section 4(a)(2) of the Securities Act or our interpretation of Section 4(a)(2), is the reason that Rule 506, ''as revised pursuant to [Section 201(a)(1)], shall continue *to be treated as* a regulation issued under section 4[(a)](2) of the Securities Act of 1933'' (emphasis added).[44] Similarly, securities issued in Rule 506(c) offerings are deemed to be ''covered securities'' for purposes of

[35] The SEC Investor Advisory Committee (''Investor Advisory Committee'') was established in April 2012 pursuant to Section 911 of the Dodd-Frank Wall Street Reform and Consumer Protection Act [Pub. L. 111–203, sec. 911, 124 Stat. 1376, 1822 (July 21, 2010)] (the ''Dodd-Frank Act'') to advise the Commission on regulatory priorities, the regulation of securities products, trading strategies, fee structures, the effectiveness of disclosure, initiatives to protect investor interests and to promote investor confidence and the integrity of the securities marketplace. The Dodd-Frank Act authorizes the Investor Advisory Committee to submit findings and recommendations for review and consideration by the Commission.

[36] To facilitate public input on JOBS Act rulemaking before the issuance of rule proposals, the Commission invited members of the public to make their views known on various JOBS Act initiatives in advance of any rulemaking by submitting comment letters to the Commission's Web site at *http://www.sec.gov/spotlight/jobsactcomments.shtml*. The comment letters relating to Section 201(a) of the JOBS Act submitted in response to this invitation are located at *http://www.sec.gov/comments/jobs-title-ii/jobs-title-ii.shtml*. The comment letters submitted in response to the Proposing Release are located at *http://www.sec.gov/comments/s7-07-12/s70712.shtml*. Many commenters submitted comment letters both before and after the issuance of the Proposing Release. Dated comment letters refer to those submitted before the issuance of the Proposing Release or by commenters that submitted multiple letters.

[37] *See, e.g.,* letters from Investor Advisory Committee; North American Securities Administrators Association, Inc. (''NASAA''); Consumer Federation of America (''Consumer Federation'').

[38] *Disqualification of Felons and Other ''Bad Actors'' from Rule 506 Offerings,* Release No. 33–9414 (July 10, 2013) (the ''Bad Actor Release'').

[39] *See Amendments to Regulation D, Form D and Rule 156,* Release No. 33–9416 (July 10, 2013).

[40] *See Non-Public Offering Exemption,* Release No. 33–4552 (Nov. 6, 1962) [27 FR 11316 (Nov. 16, 1962)].

[41] *See* Rule 502(c) and Rule 506(b)(1) of Regulation D [17 CFR 230.506(b)(1)]. The failure to comply with Rule 502(c) is deemed to be significant to the offering as a whole, which means that an issuer cannot rely on the ''insignificant deviation'' relief in Rule 508 of Regulation D for violations of Rule 502(c). *See* Rule 508(a)(2) [17 CFR 230.508(a)(2)].

[42] In this regard, we also note that bills that would have amended Section 4(a)(2) directly, rather than requiring the Commission to amend Rule 506, to permit the use of general solicitation were introduced and considered by Congress, but were not enacted. *See* Access to Capital for Job Creators, H.R. 2940, 112th Cong., 1st Sess. (2011) (proposing to amend Section 4(a)(2) by adding the phrase ''whether or not such transactions involve general solicitation or general advertising''); Access to Capital for Job Creators, S.1831, 112th Cong., 1st Sess. (2011) (same).

[43] As revised, Rule 500(c) reads as follows: ''Attempted compliance with any rule in Regulation D does not act as an exclusive election; the issuer can also claim the availability of any other applicable exemption. For instance, an issuer's failure to satisfy all the terms and conditions of rule 506*(b)* (§ 230.506*(b)*) shall not raise any presumption that the exemption provided by section 4*(a)*(2) of the Act is not available.'' (additions italicized).

[44] Section 201(a)(1) of the JOBS Act.

Section 18(b)(4)(E) of the Securities Act,[45] only by virtue of Section 201(a)(1) of the JOBS Act.

1. Proposed Rule Amendment

To implement the mandated rule change, we proposed new Rule 506(c), which would permit the use of general solicitation to offer and sell securities under Rule 506, provided that the following conditions are satisfied:

- All terms and conditions of Rule 501[46] and Rules 502(a)[47] and 502(d)[48] must be satisfied;
- all purchasers of securities must be accredited investors; and
- the issuer must take reasonable steps to verify that the purchasers of the securities are accredited investors.

Offerings under proposed Rule 506(c) would not be subject to the requirement to comply with Rule 502(c), which contains the prohibition against general solicitation. While we proposed Rule 506(c) to enable issuers to use general solicitation in Rule 506 offerings, we also preserved, in current Rule 506(b), the existing ability of issuers to conduct Rule 506 offerings subject to the prohibition against general solicitation.

2. Comments on the Proposed Rule Amendment

Commenters were sharply divided in their views on the proposed amendment to Rule 506. Commenters who supported the proposed amendment to Rule 506 stated that Rule 506(c), if adopted, would assist issuers, particularly early stage and smaller issuers, in raising capital by allowing them to solicit investments from a larger pool of investors.[49] These commenters generally approved of the flexibility afforded by the manner in which we proposed to implement Rule 506(c)'s verification requirement,[50] as further discussed below, and supported retaining, in its current form, the ability of issuers under existing Rule 506(b) to conduct Rule 506 offerings subject to the prohibition against general solicitation.[51] A number of commenters stated that they supported the availability of Rule 506(c) for private funds pursuant to the Commission's guidance in the Proposing Release.[52]

Other commenters opposed the proposed amendment to Rule 506 in its entirety or in part. Many of these commenters expressed concern that the proposed amendment, if adopted, would increase the risk of fraudulent and abusive Rule 506 offerings and asserted that additional investor safeguards are necessary under Rule 506(c).[53] A number of these commenters urged the Commission to adopt rules concerning bad actor disqualifications for Rule 506 offerings, as required by Section 926 of the Dodd-Frank Act.[54] Other commenters recommended that the Commission amend the definition of ''accredited investor'' by raising the income and net worth thresholds for natural persons or by implementing other measures of financial sophistication.[55] Some commenters stated that the Commission should condition the availability of the Rule 506(c) exemption on the filing of Form D or require the advance filing of Form D, or both.[56] Other commenters argued that the Commission should adopt specific standards or requirements that would govern the content and/or manner of general solicitations in Rule 506(c) offerings, particularly with respect to advertising by private funds.[57] A number of commenters urged the Commission to require that the materials used to generally solicit investors in Rule 506(c) offerings be filed with or furnished to either the Commission or to FINRA.[58]

A number of commenters requested that the Commission provide transitional guidance with respect to ongoing offerings under existing Rule 506 that commenced before the effectiveness of Rule 506(c).[59] For example, in some situations, the initial closings in these offerings may have already occurred, and could have included non-accredited investors pursuant to offering procedures that would not have involved any form of general solicitation.[60] Several commenters suggested that the Commission clarify that an issuer would be entitled to conduct the portion of the

[45] 15 U.S.C. 77r(b)(4)(E). This means that state blue sky registration requirements do not apply to securities offered or sold in Rule 506(c) offerings.

[46] Rule 501 sets forth definitions for the terms used in Regulation D, such as ''accredited investor.''

[47] Rule 502(a) addresses the question of integration by providing a six-month safe harbor from integration for successive Regulation D offerings and a five-factor framework to apply in cases in which the six-month safe harbor is not available.

[48] Rule 502(d) provides that, for resale purposes, securities acquired in a Regulation D offering, except as provided in Rule 504(b)(1), have the status of securities acquired in a transaction under Section 4(a)(2) of the Securities Act. Rule 144(a)(3)(ii) [17 CFR 230.144(a)(3)(ii)] defines ''restricted securities'' as securities ''acquired from the issuer that are subject to the resale limitations of § 230.502(d) under Regulation D. . . .'' Separately, Section 201(b) of the JOBS Act added Section 4(b) of the Securities Act, which provides that ''[o]ffers and sales exempt under [Rule 506 as amended pursuant to Section 201 of the JOBS Act] shall not be deemed public offerings under the Federal securities laws as a result of general advertising or general solicitation.'' Thus, securities acquired under new Rule 506(c) would also meet the definition of ''restricted securities'' under Rule 144(a)(3)(i) [17 CFR 230.144(a)(3)(i)] (''[s]ecurities acquired directly or indirectly from the issuer, or from an affiliate of the issuer, in a transaction or chain of transactions not involving any public offering'').

[49] *See, e.g.,* letters from Biotechnology Industry Organization (''BIO''); National Small Business Association (''NSBA'').

[50] *See* letters from Linklaters LLP (''Linklaters'') (stating that a ''straightforward, focused rule that provides issuers with the flexibility to continue to adapt to market practice is the best way to realize the spirit and intent of the Jumpstart Our Business Startups Act''); BlackRock (stating that ''[o]verall, we believe that the Proposed Rule is in accordance with the intent of Congress and will facilitate the formation of capital''); Securities Regulation Committee, Business Law Section of the New York State Bar Association (''SRC of NYSBA'').

[51] *See, e.g.,* letters from the Federal Regulation of Securities Committee, Business Law Section of the American Bar Association (''ABA Fed. Reg. Comm.''); Angel Capital Association (''ACA'') (Sept. 27, 2012); The CrowdFund Intermediary Regulatory Advocates (''CFIRA''); Investment Program Association (''IPA''); Montgomery & Hansen, LLP (''Montgomery & Hansen''); NSBA; Committee on Securities Regulation of the New York City Bar Association (''NYCBA''); Sullivan & Cromwell LLP (''S&C''); Securities Industry and Financial Markets Association (''SIFMA'') and The Financial Services Roundtable (''FSR'') (Oct. 5, 2012).

[52] *See, e.g.,* letters from BlackRock; Dukas Public Relations (''Dukas''); Forum for U.S. Securities Lawyers in London; Hedge Fund Association (''HFA''); Investment Adviser Association (''IAA''); Managed Funds Association (''MFA'') (Sept. 28, 2012); NYCBA; SRC of NYSBA. In the Proposing Release, we stated that private funds that engage in general solicitation under proposed Rule 506(c) would not be precluded from relying on the exclusions from the definition of ''investment company'' set forth in Section 3(c)(1) and Section 3(c)(7) of the Investment Company Act of 1940.

[53] *See, e.g.,* letters from AARP; AFL–CIO and Americans for Financial Reform (''AFR''); Sen. Levin; CFA Institute; Council of Institutional Investors (''CII''); Consumer Federation; Fund Democracy, Inc. (''Fund Democracy''); Office of the Secretary of the Commonwealth of Massachusetts Securities Division (''Massachusetts Securities Division''); NASAA.

[54] Public Law 111–203, sec. 926, 124 Stat. 1376, 1851 (July 21, 2010) (to be codified at 15 U.S.C. 77d note). *See, e.g.,* letters from AFL–CIO and AFR; Consumer Federation; Fund Democracy; Commissioner of Securities, State of Hawaii (''Hawaii Commissioner of Securities''); Investor Advisory Committee; Rep. Waters; Commissioner of Securities, State of Missouri (''Missouri Commissioner of Securities''); NASAA.

[55] *See, e.g.,* letters from AARP; AFL–CIO and AFR; BetterInvesting; CFA Institute; Consumer Federation; Investor Advisory Committee; Investment Company Institute (''ICI''); Rep. Waters; Massachusetts Securities Division (July 2, 2012).

[56] *See, e.g.,* letters from AARP; AFL–CIO and AFR; Consumer Federation; Hawaii Commissioner of Securities; Investor Advisory Committee; Massachusetts Securities Division (July 2, 2012); Missouri Commissioner of Securities; Commissioner of Securities and Insurance, State of Montana (''Montana Commissioner of Securities''); NASAA; Ohio Division of Securities.

[57] *See, e.g.,* letters from Sen. Levin; Consumer Federation; ICI; Independent Directors Council (''IDC''); Rep. Waters; Montana Commissioner of Securities; NASAA.

[58] *See, e.g.,* letters from AFL–CIO and AFR; Investor Advisory Committee; ICI; Massachusetts Securities Division (July 2, 2012).

[59] *See* letters from ABA Fed. Reg. Comm.; Forum for U.S. Securities Lawyers in London; S&C; IPA.

[60] *See* letter from ABA Fed. Reg. Comm.

offering following the effectiveness of Rule 506(c) in accordance with the requirements of new Rule 506(c), without the portion of the offering occurring after the rule's effectiveness affecting the portion of the offering that was completed prior to the rule's effectiveness.[61]

3. Final Rule Amendment

After considering the comments, we are adopting Rule 506(c) as proposed, with one modification. Under new Rule 506(c), issuers can offer securities through means of general solicitation, provided that they satisfy all of the conditions of the exemption.[62] These conditions are:

- all terms and conditions of Rule 501 and Rules 502(a) and 502(d) must be satisfied;[63]
- all purchasers of securities must be accredited investors;[64] and
- the issuer must take reasonable steps to verify that the purchasers of the securities are accredited investors.[65]

Issuers relying on Rule 506(c) for their offerings will not be subject to the prohibition against general solicitation found in Rule 502(c).[66] In addition and as further discussed below, in response to comments from a wide range of commenters asking for greater certainty with respect to satisfying the verification requirement, we are also including in Rule 506(c) a non-exclusive list of methods that issuers may use to verify the accredited investor status of natural persons.

Issuers will continue to have the ability under Rule 506(b) to conduct Rule 506 offerings subject to the prohibition against general solicitation. As we noted in the Proposing Release, offerings under existing Rule 506(b) represent an important source of capital for issuers of all sizes, and we believe that the continued availability of existing Rule 506(b) will be important for those issuers that either do not wish to engage in general solicitation in their Rule 506 offerings (and become subject to the requirement to take reasonable steps to verify the accredited investor status of purchasers) or wish to sell privately to non-accredited investors who meet Rule 506(b)'s sophistication requirements. Retaining the safe harbor under existing Rule 506(b) may also be beneficial to investors with whom an issuer has a pre-existing substantive relationship.[67] In this regard, we do not believe that Section 201(a) requires the Commission to modify Rule 506 to impose any new requirements on offers and sales of securities that do not involve general solicitation. Therefore, the amendment to Rule 506 we are adopting today does not amend or modify the requirements relating to existing Rule 506(b).

Finally, with respect to transition matters, for an ongoing offering under Rule 506 that commenced before the effective date of Rule 506(c), the issuer may choose to continue the offering after the effective date in accordance with the requirements of either Rule 506(b) or Rule 506(c). If an issuer chooses to continue the offering in accordance with the requirements of Rule 506(c), any general solicitation that occurs after the effective date will not affect the exempt status of offers and sales of securities that occurred prior to the effective date in reliance on Rule 506(b).

B. Reasonable Steps To Verify Accredited Investor Status

Section 201(a)(1) of the JOBS Act mandates that our amendment to Rule 506 require issuers using general solicitation in Rule 506 offerings ''to take reasonable steps to verify that purchasers of the securities are accredited investors, using such methods as determined by the Commission.'' As noted in the Proposing Release, we believe that the purpose of the verification mandate is to address concerns, and reduce the risk, that the use of general solicitation in Rule 506 offerings could result in sales of securities to investors who are not, in fact, accredited investors.[68]

1. Proposed Rule Amendment

To implement the verification mandate of Section 201(a)(1), we proposed to condition the Rule 506(c) exemption on the requirement that issuers using general solicitation ''take reasonable steps to verify'' that the purchasers of the offered securities are accredited investors. As proposed, whether the steps taken are ''reasonable'' would be an objective determination by the issuer (or those acting on its behalf), in the context of the particular facts and circumstances of each purchaser and transaction. Under this principles-based approach, issuers would consider a number of factors when determining the reasonableness of the steps to verify that a purchaser is an accredited investor, such as:

- 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 in which the purchaser was solicited to participate in the offering, and the terms of the offering, such as a minimum investment amount.

These factors would be interconnected, and the information gained by looking at these factors would help an issuer assess the reasonable likelihood that a potential purchaser is an accredited investor, which would, in turn, affect the types of steps that would be reasonable to take to verify a purchaser's accredited investor status.

In the Proposing Release, we considered providing a list of specified methods for satisfying the verification requirement, which was suggested by some commenters on Section 201(a) prior to the issuance of the Proposing Release.[69] We expressed concern that, in

[61] *See* letters from ABA Fed. Reg. Comm.; S&C (stating that ''[w]e believe that such issuers should be allowed, upon effectiveness of the final rule, to use the new Rule 506(c) exemption and use general solicitation for the remaining portion of their offerings, provided that they satisfy the requirements of Rule 506(c) going forward.'').

[62] We also note that broker-dealers participating in offerings in conjunction with issuers relying on Rule 506(c) would continue to be subject to FINRA rules regarding communications with the public, which, among other things, (1) generally require all member communications to be based on principles of fair dealing and good faith, to be fair and balanced, and to provide a sound basis for evaluating the facts in regard to any particular security or type of security, industry or service; and (2) prohibit broker-dealers from making false, exaggerated, unwarranted, promissory or misleading statements or claims in any communications. *See* FINRA Rule 2210.

[63] New Rule 506(c)(1).

[64] New Rule 506(c)(2)(i).

[65] New Rule 506(c)(2)(ii).

[66] Offerings under Rule 506(c) will also not be subject to the information requirements in Rule 502(b) for non-accredited investors, because all purchasers in Rule 506(c) offerings are required to be accredited investors.

[67] *See* Release No. 33–7856, at 25852 (noting that ''one method of ensuring that general solicitation is not involved is to establish the existence of a 'pre-existing, substantive relationship'" and that ''there may be facts and circumstances in which a third party, other than a registered broker-dealer, could established a 'pre-existing, substantive relationship' sufficient to avoid a 'general solicitation' '').

[68] *See, e.g., Markup of H.R. 2940, Access to Capital for Job Creators Act,* Subcommittee on Capital Markets and Government Sponsored Enterprises, House Financial Services Committee, 112th Cong. (Oct. 5, 2011) (remarks of Rep. Waters, explaining that she is introducing the amendment that requires issuers to take reasonable steps to verify accredited investor status because ''we must take steps to ensure that those folks are indeed sophisticated''); 157 Cong. Rec. H7291 (daily ed. Nov. 3, 2011) (remarks of Rep. Maloney (same)); 157 Cong. Rec. H7294 (daily ed. Nov. 3, 2011) (remarks of Rep. Lee (same)).

[69] *See* letters from MFA (June 26, 2012) (suggesting that the Commission publish a non-exclusive list of the types of third-party evidence that an investor could provide to establish accredited investor status, in conjunction with certifying that he or she is an accredited investor); NASAA (July 3, 2012) (recommending that the Commission set forth non-exclusive safe harbors to specify the types of actions that would be deemed

designating such a list—for example, by setting forth particular types of information that issuers may rely upon as conclusive means of verifying accredited investor status—there may be circumstances where such information will not actually verify accredited investor status or where issuers may unreasonably overlook or disregard other information indicating that a purchaser is not, in fact, an accredited investor. Also, we were concerned that requiring issuers to use specified methods of verification would be impractical, burdensome and potentially ineffective in light of the numerous ways in which a purchaser can qualify as an accredited investor, as well as the potentially wide range of verification issues that may arise, depending on the nature of the purchaser and the facts and circumstances of a particular Rule 506(c) offering. Even if the list of specified methods was not mandatory, but rather, constituted a non-exclusive list, we were concerned that a non-exclusive list of specified methods could be viewed by market participants as, in effect, required methods, in which compliance with at least one of the enumerated methods could be viewed as necessary in all circumstances to demonstrate that the verification requirement has been satisfied, thereby eliminating the flexibility that proposed Rule 506(c) was intended to provide.

We requested comment in the Proposing Release on our proposed principles-based method and its effectiveness in limiting sales of securities in Rule 506(c) offerings to only accredited investors. We also requested comment on possible alternative approaches for implementing the verification mandate of Section 201(a)(1), such as a rule that specifies mandatory methods for verifying accredited investor status or a non-exclusive list of verification methods that would function as a safe harbor for compliance with the verification requirement.

2. Comments on the Proposed Rule Amendment

Commenters expressed a wide range of views on the proposed approach to the verification requirement in Rule 506(c). Some commenters commended the Commission for proposing a flexible, principles-based standard for verification.[70] For example, one commenter stated that the Commission's proposed approach would provide issuers with the flexibility to develop tailored, reliable and cost-effective procedures for verification.[71] A number of commenters stated that the discussion in the Proposing Release of the factors that issuers may take into account in verifying accredited investor status would assist issuers in assessing the reasonableness of their verification processes.[72] Other commenters asserted that not requiring issuers to use certain specified methods to verify a purchaser's accredited investor status would permit advancements in verification methods over time.[73] Some commenters expressed support for the Commission's proposal that accredited investor status may be verified through an attestation or certification by a third party, provided that the issuer has a reasonable basis to rely on such third-party verification.[74]

Other commenters opposed the Commission's proposed approach, for various reasons. A number of these commenters opposed the proposed verification standard because, in their view, self-certification by itself should be sufficient to satisfy the verification requirement.[75] Some commenters opposed the proposed verification standard because it did not prescribe specific verification methods, which they believed is required in order to satisfy the verification mandate in Section 201(a).[76] One commenter stated that the Commission should deem the verification requirement to be satisfied if all purchasers in a Rule 506(c) offering are in fact accredited investors.[77] Another commenter stated that verification of accredited investor status should not be a condition of the Rule 506(c) exemption when the purchaser is actually an accredited investor.[78]

Commenters expressed differing views on whether the Commission should include a non-exclusive list of methods in proposed Rule 506(c) for satisfying the verification requirement. Many commenters, encompassing a wide range of perspectives (*e.g.,* state government officials, law firms, investor organizations, professional and trade associations, and individuals), urged the Commission to provide such a non-exclusive list.[79] A number of these commenters cited the lack of legal certainty that the verification requirement has been satisfied in any given situation as the reason why, in their view, the Commission should include a non-exclusive list of verification methods in Rule 506(c).[80] In contrast, other commenters stated that the Commission should not include a non-exclusive list of verification methods in Rule 506(c), arguing that such a list could be viewed by market participants as the required verification methods, which would thereby undermine the flexibility of the Commission's proposed approach.[81]

If there were to be a non-exclusive list of verification methods, commenters expressed a range of views on what should be included in such a list, such as verification by certain third parties or through tax returns and third-party documentary proof such as Forms W–2, Forms 1099, bank statements, brokerage account statements, tax assessment valuations and appraisal reports.[82] With

''reasonable steps to verify'' for three types of accredited investors: natural persons who purport to satisfy the income test; natural persons who purport to satisfy the net worth test; and entities who purport to meet one of the other tests set forth in Rule 501(a)).

[70] *See, e.g.,* letters from HFA; MFA (Sept. 28, 2012); BIO; ABA Fed. Reg. Comm.; IAA; Linklaters; NYCBA; SRC of NYSBA; SIFMA and FSR (Oct. 5, 2012); Artivest Holdings, Inc. (''Artivest'').

[71] *See* letter from SIFMA and FSR (Oct. 5, 2012).

[72] *See, e.g.,* letters from SRC of NYSBA; S&C; SIFMA and FSR (Oct. 5, 2012); IAA.

[73] *See* letters from ACA (Sept. 27, 2012); CFIRA.

[74] *See, e.g.,* letters from IAA; SIFMA and FSR (Oct. 5, 2012); Tannenbaum Helpern Syracuse & Hirschtritt LLP (''Tannenbaum Helpern''). A number of commenters noted that the availability of third-party verification could address investors' privacy and security concerns in providing information to an issuer. *See, e.g.,* letters from L. Neumann; NSBA. One commenter urged the Commission not to limit third-party verification providers to certain types of entities. *See* letter from Tannenbaum Helpern. One commenter suggested the possibility of requiring investors to self-certify as to accredited investor status under penalty of perjury. *See* letter from NSBA.

[75] *See, e.g.,* letters from C. Hague; G. Brooks; Golenbock Eiseman Assor Bell & Peskoe LLP; P. Christenson; W. Johnson.

[76] *See, e.g.,* letters from AFL–CIO and AFR; Sen. Levin; Consumer Federation; Fund Democracy; Rep. Waters; Massachusetts Securities Division; The Options Clearing Corporation (''OCC''); Ohio Division of Securities.

[77] *See* letter from IPA.

[78] *See* letter from S. Keller.

[79] *See, e.g.,* letters from ACA (Sept. 27, 2012 and Dec. 11, 2012); BIO; CFIRA; HFA; Hawaii Commissioner of Securities; IAA; Investor Advisory Committee (stating that the ''facts and circumstances'' based approach proposed by the Commission does not do enough either to ensure only accredited investors purchase in the offering or to provide issuers with the certainty they need to develop appropriate procedures); J. McLaughlin; MFA (Sept. 28, 2012); Montana Commissioner of Securities; NASAA; Tufts Stephenson & Kasper, LLP; Nevada Securities Division; OCC; Ohio Division of Securities; Pepper Hamilton LLP (''Pepper Hamilton''); Plexus Consulting Group, LLC (''Plexus Consulting Group''); Small Business Investor Association (''SBIA''); South Carolina Securities Commissioner; Virginia Division of Securities.

[80] *See, e.g.,* letters from ACA (Sept. 27, 2012 and Dec. 11, 2012); HFA; Investor Advisory Committee; OCC.

[81] *See, e.g.,* letters from ABA Fed. Reg. Comm.; Artivest; BlackRock; S&C; SIFMA and FSR (Oct. 5, 2012).

[82] *See, e.g.,* letters from B. Methven; L. Neumann; NASAA.

respect to the types of third parties that could provide verification services, commenters named registered brokers-dealers,[83] banks and other financial institutions,[84] registered investment advisers,[85] certified financial planners,[86] attorneys,[87] and accountants.[88] Other commenters suggested including in a non-exclusive list of verification methods self-certification, plus a minimum investment amount such as $25,000,[89] $100,000,[90] $250,000,[91] $500,000[92] or $1,000,000.[93]

In contrast, one commenter argued that the ability to satisfy a minimum investment amount would not necessarily mean a person is an accredited investor, but rather, that the investor could be ''over-concentrated in the investment.''[94] Another commenter stated that the verification requirement should not be deemed satisfied simply because an issuer possesses general information about the average compensation in the investor's profession or workplace.[95]

Several commenters stated that there should be a ''grandfather'' provision from the verification mandate for an issuer's existing investors who purchased securities in a Rule 506(b) offering prior to the effective date of Rule 506(c),[96] and one commenter proposed to limit the scope of any grandfather provision to only existing accredited investors.[97] Two of these commenters reasoned that, as issuers are prohibited from engaging in general solicitation activities in Rule 506(b) offerings, their existing investors did not purchase securities in offerings that used general solicitation, and any future investments by these investors would be based on their pre-existing relationship with the issuers, and not as a result of general solicitation.[98] Therefore, a grandfather provision would be appropriate because the purpose of the verification mandate in Section 201(a) of the JOBS Act is to require the verification of the accredited investor status of only prospective purchasers who come to the issuer ''as a result of'' the issuer's general solicitation activities.[99] One commenter stated that, for existing investors, a ''reaffirmation representation'' of accredited investor status received shortly before or simultaneously with any subsequent investment should be sufficient for Rule 506(c) purposes.[100]

3. Final Rule Amendment

After considering the comments and as directed by Section 201(a) of the JOBS Act, we are adopting as a condition of new Rule 506(c) the requirement that issuers take ''reasonable steps to verify'' that purchasers of the offered securities are accredited investors. This requirement is separate from and independent of the requirement that sales be limited to accredited investors, and must be satisfied even if all purchasers happen to be accredited investors.[101] We are also including in Rule 506(c) a non-exclusive list of methods that issuers may use to satisfy the verification requirement. As discussed above, a number of commenters urged the Commission to provide greater certainty for issuers that the verification requirement has been satisfied by providing a non-exclusive list of methods for verifying the accredited investor status of purchasers in Rule 506(c) offerings. Upon further consideration, we have concluded that a general requirement that issuers take ''reasonable steps to verify'' that the purchasers are accredited investors, combined with a non-exclusive list of verification methods that are deemed to meet this requirement, would maintain the flexibility of the verification standard while providing additional clarity and certainty that this requirement has been satisfied if one of the specified methods is used. We have specified methods for verifying the accredited investor status of natural persons because we believe that the potential for uncertainty and the risk of participation by non-accredited investors is highest in offerings involving natural persons as purchasers.

a. Principles-Based Method of Verification

Under Rule 506(c), issuers are required to take reasonable steps to verify the accredited investor status of purchasers. Consistent with the Proposing Release, whether the steps taken are ''reasonable'' will be an objective determination by the issuer (or those acting on its behalf), in the context of the particular facts and circumstances of each purchaser and transaction. Among the factors that issuers should consider under this facts and circumstances analysis are:

- 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 in which the purchaser was solicited to participate in the offering, and the terms of the offering, such as a minimum investment amount.

As noted in the Proposing Release, these factors are interconnected and are intended to help guide an issuer in assessing the reasonable likelihood that a purchaser is an accredited investor—which would, in turn, affect the types of steps that would be reasonable to take to verify a purchaser's accredited investor status. After consideration of the facts and circumstances of the purchaser and of the transaction, the more likely it appears that a purchaser qualifies as an accredited investor, the fewer steps the issuer would have to take to verify accredited investor status, and vice versa. For example, if the terms of the offering require a high minimum investment amount and a purchaser is able to meet those terms, then the likelihood of that purchaser satisfying the definition of accredited investor may be sufficiently high such that, absent any facts that indicate that the purchaser is not an accredited investor, it may be reasonable for the issuer to take fewer steps to verify or, in certain cases, no additional steps to verify accredited investor status other than to confirm that the purchaser's cash

[83] *See, e.g.,* letters from Massachusetts Securities Division (July 2, 2012); J. McLaughlin; NASAA; OCC; Pepper Hamilton; Plexus Consulting Group; SBIA.

[84] *See* letter from Massachusetts Securities Division (July 2, 2012).

[85] *See, e.g.,* letters from Plexus Consulting Group; SBIA.

[86] *See, e.g.,* letters from Plexus Consulting Group; NSBA (stating that ''if there must be some kind of enhanced verification, we recommend that a certification by the investor's attorney, CPA, certified financial advisor or other licensed professional should be sufficient'').

[87] *Id.*

[88] *Id.*

[89] *See* letter from Montgomery & Hansen.

[90] *See* letters from B. Methven; SBIA (provided the issuer is a small business investment company (''SBIC'') or a fund that has been authorized to apply to be an SBIC by the U.S. Small Business Administration).

[91] *See* letter from J. Joseph (stating that ''[s]ome may feel that that number is $25,000, perhaps $100,000 but certainly at $250,000 there should be no question that the investor is properly qualified and accredited'').

[92] *See* letter from MFA (Sept. 28, 2012) (stating that ''[i]n considering the appropriate minimum investment level, we have previously recommended a minimum investment level of 50% of the accredited investor net worth or total asset thresholds, currently $500,000 for an individual, and $2,500,000 for an entity'').

[93] *See* letter from Pepper Hamilton.

[94] Letter from Massachusetts Securities Division (July 2, 2012).

[95] *See* letter from NASAA.

[96] *See* letters from MFA (Sept. 28, 2012); IAA; Tannenbaum Helpern.

[97] *See* letter from Pepper Hamilton.

[98] *See* letters from MFA (Sept. 28, 2012); Tannenbaum Helpern.

[99] *See* letter from Tannenbaum Helpern.

[100] *See* letter from Pepper Hamilton.

[101] This will avoid diminishing the incentive for issuers to undertake the reasonable verification steps envisioned by the statute.

investment is not being financed by a third party.

Regardless of the particular steps taken, because the issuer has the burden of demonstrating that its offering is entitled to an exemption from the registration requirements of Section 5 of the Securities Act,[102] it will be important for issuers and their verification service providers to retain adequate records regarding the steps taken to verify that a purchaser was an accredited investor.

Nature of the Purchaser. In determining the reasonableness of the steps to verify accredited investor status, an issuer should consider the nature of the purchaser of the offered securities. The definition of ''accredited investor'' in Rule 501(a) includes natural persons and entities that come within any of eight enumerated categories in the rule, or that the issuer reasonably believes come within one of those categories, at the time of the sale of securities to that natural person or entity. Some purchasers may be accredited investors based on their status, such as:

- a broker or dealer registered pursuant to Section 15 of the Securities Exchange Act of 1934 (the ''Exchange Act''); [103] or
- an investment company registered under the Investment Company Act of 1940 (the ''Investment Company Act'') or a business development company as defined in Section 2(a)(48) of that Act.[104]

Some purchasers may be accredited investors based on a combination of their status and the amount of their total assets, such as:

- a plan established and maintained by a state, its political subdivisions, or any agency or instrumentality of a state or its political subdivisions, for the benefit of its employees, if such plan has total assets in excess of $5 million; [105] or
- an Internal Revenue Code (''IRC'') Section 501(c)(3) organization, corporation, Massachusetts or similar business trust, or partnership, not formed for the specific purpose of acquiring the securities offered, with total assets in excess of $5 million.[106]

Natural persons may be accredited investors based on either their net worth or their annual income, as follows:

- a natural person whose individual net worth, or joint net worth with that person's spouse, exceeds $1 million, excluding the value of the person's primary residence; [107] or
- a natural person who had an individual income in excess of $200,000 in each of the two most recent years, or joint income with that person's spouse in excess of $300,000 in each of those years, and has a reasonable expectation of reaching the same income level in the current year.[108]

As Rule 501(a) sets forth different categories of accredited investors, an issuer should recognize that the steps that will be reasonable to verify whether a purchaser is an accredited investor will vary depending on the type of accredited investor that the purchaser claims to be. For example, the steps that may be reasonable to verify that an entity is an accredited investor by virtue of being a registered broker-dealer—such as by going to FINRA's BrokerCheck Web site [109]—will necessarily differ from the steps that may be reasonable to verify whether a natural person is an accredited investor.

As we stated in the Proposing Release, the verification of natural persons as accredited investors may pose greater practical difficulties as compared to other categories of accredited investors, particularly for natural persons claiming to be accredited investors based on the net worth test. These practical difficulties likely will be exacerbated by privacy concerns about the disclosure of personal financial information. As between the net worth test and the income test for natural persons, we recognize that commenters have suggested that it might be more difficult for an issuer to obtain information about the assets and liabilities that determine a person's net worth—particularly the liabilities—than it would be to obtain information about a person's annual income,[110] although there could be privacy concerns with respect to either test. The question of what type of information would be sufficient to constitute reasonable steps to verify accredited investor status under the particular facts and circumstances will also depend on other factors, as described below.

Information about the Purchaser. The amount and type of information that an issuer has about a purchaser can also be a significant factor in determining what additional steps would be reasonable to take to verify the purchaser's accredited investor status. The more information an issuer has indicating that a prospective purchaser is an accredited investor, the fewer steps it may have to take, and vice versa.[111] Examples of the types of information that issuers could review or rely upon—any of which might, depending on the circumstances, in and of themselves constitute reasonable steps to verify a purchaser's accredited investor status—include, without limitation:

- publicly available information in filings with a federal, state or local regulatory body—for example, without limitation:
  - ○ the purchaser is a named executive officer of an Exchange Act registrant, and the registrant's proxy statement discloses the purchaser's compensation; or
  - ○ the purchaser claims to be an IRC Section 501(c)(3) organization with $5 million in assets, and the organization's Form 990 series return filed with the Internal Revenue Service discloses the organization's total assets; [112]
- third-party information that provides reasonably reliable evidence that a person falls within one of the enumerated categories in the accredited investor definition—for example, without limitation:
  - ○ the purchaser is a natural person and provides copies of pay stubs for the two most recent years and the current year; or
  - ○ specific information about the average compensation earned at the purchaser's workplace by persons at the level of the purchaser's seniority is publicly available; or
- verification of a person's status as an accredited investor by a third party, provided that the issuer has a

[102] *SEC* v. *Ralston Purina,* 346 U.S. 119, 126 (1953) (''Keeping in mind the broadly remedial purposes of federal securities legislation, imposition of the burden of proof on an issuer who would plead the exemption seems to us fair and reasonable.'').

[103] *See* 17 CFR 230.501(a)(1).

[104] *See id.*

[105] *See id.*

[106] *See* 17 CFR 230.501(a)(3).

[107] *See* 17 CFR 230.501(a)(5).

[108] *See* 17 CFR 230.501(a)(6).

[109] This Web site is available at: *http://www.finra.org/Investors/ToolsCalculators/BrokerCheck/.*

[110] *See* letters from NASAA (stating that ''[v]erification of net worth is more challenging because an individual could provide proof of assets but not liabilities.''); P. Sigelman (Sept. 28, 2012).

[111] If an issuer has actual knowledge that the purchaser is an accredited investor, then the issuer will not have to take any steps at all.

[112] Such an organization is required to make the Form 990 series returns available for public inspection. *See* Internal Revenue Service, *Public Disclosure and Availability of Exempt Organizations Returns and Applications: Documents Subject to Public Disclosure,* available at: *http://www.irs.gov/Charities-&-Non-Profits/Public-Disclosure-and-Availability-of-Exempt-Organizations-Returns-and-Applications:-Documents-Subject-to-Public-Disclosure* (last reviewed or updated April 28, 2013).

reasonable basis to rely on such third-party verification.[113]

Nature and Terms of the Offering. The nature of the offering—such as the means through which the issuer publicly solicits purchasers—may be relevant in determining the reasonableness of the steps taken to verify accredited investor status. An issuer that solicits new investors through a Web site accessible to the general public, through a widely disseminated email or social media solicitation, or through print media, such as a newspaper, will likely be obligated to take greater measures to verify accredited investor status than an issuer that solicits new investors from a database of pre-screened accredited investors created and maintained by a reasonably reliable third party. We believe that an issuer will be entitled to rely on a third party that has verified a person's status as an accredited investor, provided that the issuer has a reasonable basis to rely on such third-party verification. We do not believe that an issuer will have taken reasonable steps to verify accredited investor status if it, or those acting on its behalf, required only that a person check a box in a questionnaire or sign a form, absent other information about the purchaser indicating accredited investor status.

The terms of the offering will also affect whether the verification methods used by the issuer are reasonable. We continue to believe that there is merit to the view that a purchaser's ability to meet a high minimum investment amount could be a relevant factor to the issuer's evaluation of the types of steps that would be reasonable to take in order to verify that purchaser's status as an accredited investor. By way of example, the ability of a purchaser to satisfy a minimum investment amount requirement that is sufficiently high such that only accredited investors could reasonably be expected to meet it, with a direct cash investment that is not financed by the issuer or by any third party, could be taken into consideration in verifying accredited investor status.

Commenters suggested a number of alternative approaches to implementing the verification mandate. Some commenters urged us to adopt a requirement that prescribes specific methods of verification that issuers must use, either because they believed such methods are needed for issuers seeking clarity on how to comply with this condition of Rule 506(c)[114] or because they believed that such methods are needed to maintain investor protection.[115] We have decided not to take such an approach. As we stated in the Proposing Release, we believe that, at present, requiring issuers to use specified methods of verification will be impractical and potentially ineffective in light of the numerous ways in which a purchaser can qualify as an accredited investor, as well as the potentially wide range of verification issues that may arise, depending on the nature of the purchaser and the facts and circumstances of a particular Rule 506(c) offering. We are also concerned that a prescriptive rule that specifies required verification methods could be overly burdensome in some cases, by requiring issuers to follow the same steps, regardless of their particular circumstances, and ineffective in others, by requiring steps that, in the particular circumstances, would not actually verify accredited investor status.

We believe that the approach we are adopting appropriately addresses the concerns underlying the verification mandate by obligating issuers to take reasonable steps to verify that the purchasers are accredited investors, but not requiring them to follow uniform verification methods that may be ill-suited or unnecessary to a particular offering or purchaser in light of the facts and circumstances. We also expect that such an approach will give issuers and market participants the flexibility to adopt different approaches to verification depending on the circumstances, to adapt to changing market practices, and to implement innovative approaches to meeting the verification requirement, such as the development of reliable third-party databases of accredited investors and verification services. In addition, we anticipate that many practices currently used by issuers in connection with existing Rule 506 offerings will satisfy the verification requirement for offerings pursuant to Rule 506(c).

b. Non-Exclusive Methods of Verifying Accredited Investor Status

In addition to adopting a principles-based method of verification, we are including in Rule 506(c) four specific non-exclusive methods of verifying accredited investor status for natural persons that, if used, are deemed to satisfy the verification requirement in Rule 506(c); provided, however, that none of these methods will be deemed to satisfy the verification requirement if the issuer or its agent has knowledge that the purchaser is not an accredited investor.[116] While the principles-based method of verification is intended to provide an issuer with the flexibility to address the particular facts and circumstances surrounding its offering, we appreciate the view of some commenters that the final rule should include a non-exclusive list of specific verification methods for natural persons that may be relied upon by those issuers seeking greater certainty that they satisfy the rule's verification requirement.[117] Accordingly, we are adding a non-exclusive list of specific verification methods to supplement our principles-based framework for verifying accredited investor status.[118] Issuers are not required to use any of the methods discussed below, and can apply the reasonableness standard directly to the specific facts and circumstances presented by the offering and the investors.[119]

[113] For example, in the future, services may develop that verify a person's accredited investor status for purposes of new Rule 506(c) and permit issuers to check the accredited investor status of possible investors, particularly for web-based Rule 506 offering portals that include offerings for multiple issuers. This third-party service, as opposed to the issuer itself, could obtain appropriate documentation or otherwise take reasonable steps to verify accredited investor status. Several commenters, in fact, have recommended that the Commission take action to facilitate the ability of issuers to rely on third parties to perform the necessary verification. *See* letters from NASAA (July 3, 2012) (recommending that the Commission allow an issuer to obtain the necessary verification through registered broker-dealers, provided that there are independent liability provisions for failure to adequately perform the verification); Massachusetts Securities Division (July 2, 2012) (urging the Commission to adopt as a safe harbor or best practice the use of an independent party, such as a broker-dealer, bank, or other financial institution, that would verify the accredited investor status of purchasers). One commenter, however, expressed concerns that some of the Web sites that currently offer lists of accredited investors could be used to facilitate fraud, noting that some offer lists based on "ethnicity, gender, and lifestyle—presumably to make [it] easier for scammers to relate to marks—and ominously, 'seniors.' " Letter from I. Moscovitz and J. Maxfield (June 27, 2012).

[114] *See, e.g.,* letter from Handler Thayer, LLP.

[115] *See, e.g.,* letters from AARP; CII.

[116] Because an issuer must have a reasonable belief that the purchaser is an accredited investor, the issuer could not form such reasonable belief if it has knowledge that the purchaser is not an accredited investor. See Section II.C of this release for a discussion of the reasonable belief standard in the definition of accredited investor in Rule 501(a).

[117] *See, e.g.,* letters from ACA (Sept. 27, 2012 and Dec. 11, 2012); Investor Advisory Committee; MFA (Sept. 28, 2012).

[118] Information and documentation collected for these verification purposes may be subject to federal and/or state privacy and data security requirements. *See, e.g.,* Regulation S–P [17 CFR 248.1–248.30] (implementing notice requirements and restrictions on a financial institution's ability to disclose nonpublic personal information about customers); *Privacy of Consumer Financial Information (Regulation S–P),* Release No. 34–42974 (June 22, 2000) [65 FR 40334 (June 29, 2000)].

[119] We expect that many issuers will conduct Rule 506(c) offerings in reliance on the principles-based method of verification, in light of its flexibility and efficiency.

First, in verifying whether a natural person is an accredited investor on the basis of income, an issuer is deemed to satisfy the verification requirement in Rule 506(c) by reviewing copies of any Internal Revenue Service (''IRS'') form that reports income, including, but not limited to, a Form W–2 (''Wage and Tax Statement''), Form 1099 (report of various types of income), Schedule K–1 of Form 1065 (''Partner's Share of Income, Deductions, Credits, etc.''), and a copy of a filed Form 1040 (''U.S. Individual Income Tax Return''),[120] for the two most recent years, along with obtaining a written representation from such person that he or she has a reasonable expectation of reaching the income level necessary to qualify as an accredited investor during the current year. In the case of a person who qualifies as an accredited investor based on joint income with that person's spouse, an issuer would be deemed to satisfy the verification requirement in Rule 506(c) by reviewing copies of these forms for the two most recent years in regard to, and obtaining written representations from, both the person and the spouse.

Second, in verifying whether a natural person is an accredited investor on the basis of net worth, an issuer is deemed to satisfy the verification requirement in Rule 506(c) by reviewing one or more of the following types of documentation, dated within the prior three months,[121] and by obtaining a written representation from such person that all liabilities necessary to make a determination of net worth have been disclosed. In the case of a person who qualifies as an accredited investor based on joint net worth with that person's spouse, an issuer would be deemed to satisfy the verification requirement in Rule 506(c) by reviewing such documentation in regard to, and obtaining representations from, both the person and the spouse. For assets: Bank statements, brokerage statements and other statements of securities holdings, certificates of deposit, tax assessments and appraisal reports issued by independent third parties are deemed to be satisfactory; and for liabilities: A consumer report (also known as a credit report) from at least one of the nationwide consumer reporting agencies is required.[122] Commenters did not provide examples of any other type of documentation that would, in our view, adequately evidence liabilities.[123] We recognize that it will be difficult for an issuer to determine whether it has a complete picture of a natural person's liabilities, and therefore, for purposes of this method, consistent with the suggestions of some commenters, we are requiring a consumer report and a written representation from such person that all liabilities necessary to make a determination of net worth have been disclosed.

Third, an issuer is deemed to satisfy the verification requirement in Rule 506(c) by obtaining a written confirmation from a registered broker-dealer, an SEC-registered investment adviser, a licensed attorney, or a certified public accountant that such person or entity has taken reasonable steps to verify that the purchaser is an accredited investor within the prior three months and has determined that such purchaser is an accredited investor.[124] While third-party confirmation by one of these parties will be deemed to satisfy the verification requirement in Rule 506(c), depending on the circumstances, an issuer may be entitled to rely on the verification of accredited investor status by a person or entity other than one of these parties, provided that any such third party takes reasonable steps to verify that purchasers are accredited investors and has determined that such purchasers are accredited investors, and the issuer has a reasonable basis to rely on such verification.

Fourth, with respect to any natural person who invested in an issuer's Rule 506(b) offering as an accredited investor prior to the effective date of Rule 506(c) and remains an investor of the issuer, for any Rule 506(c) offering conducted by the same issuer, the issuer is deemed to satisfy the verification requirement in Rule 506(c) with respect to any such person by obtaining a certification by such person at the time of sale that he or she qualifies as an accredited investor.

We are including the first three methods in our non-exclusive list of methods that are deemed to satisfy the verification requirement in Rule 506(c) because we believe that there will likely be few instances in which they would not constitute reasonable steps to verify accredited investor status. With respect to the verification method for the income test, there are numerous penalties for falsely reporting information in an Internal Revenue Service form, and these forms are filed with the Internal Revenue Service for purposes independent of investing in a Rule 506(c) offering. Similarly, we believe that the various forms of documentation set forth in the verification method for the net worth test ordinarily are generated for reasons other than to invest in a Rule 506(c) offering (with the possible exception of appraisal reports) and, in combination with a consumer report and a written representation from the investor regarding his or her liabilities, constitute sufficiently reliable evidence that such person's net worth exceeds $1 million, excluding the value of the person's primary residence. With respect to the third-party verification method, we have included written confirmations from certain third parties in our non-exclusive list of verification methods because these third parties are subject to various regulatory and/or licensing requirements. Registered broker-dealers [125] and SEC-registered investment advisers [126] are regulated by

[120] A person could provide a redacted version of an Internal Revenue Service form so as to disclose only information about annual income and to avoid disclosure of personally identifiable information, such as a Social Security number, or other information that would not be relevant to the determination of a person's annual income.

[121] A person could provide redacted versions of these documents so as to disclose only information about the amounts of assets and liabilities and to avoid disclosure of personally identifiable information, such as a Social Security number, or other information that would not be relevant to the determination of a person's net worth.

[122] We note that the Fair Credit Reporting Act (''FCRA'') [15 U.S.C. 1681 *et seq.*] requires each of the nationwide consumer reporting agencies to provide a person with a free copy of his or her consumer report, upon request, once every 12 months. In addition, the FCRA permits third parties to access individual consumer reports with the written permission of the individual.

[123] One commenter suggested that the Commission ''require the issuer to obtain a list of liabilities from the investor, which would include a sworn statement that all material liabilities are disclosed.'' Letter from NASAA. Another commenter noted that liabilities can be cross checked against UCC 1 filings, bankruptcy information on Public Access to Court Electronic Records (PACER), and credit reports. *See* letter from P. Sigelman (Sept. 28, 2012).

[124] For purposes of this method, a licensed attorney must be in good standing under the laws of the jurisdictions in which the attorney is admitted to practice law, and a certified public accountant must be in good standing under the laws of the place of the accountant's residence or principal office.

[125] Registered broker-dealers are subject to a comprehensive system of oversight by the Commission as well as FINRA. In particular, registered broker-dealers, among other things, must maintain and preserve specified books and records, develop effective supervisory policies and controls, and comply with FINRA rules regarding registration and qualification requirements for their associated persons as well as general and specific conduct rules. In addition, registered broker-dealers are subject to examinations by both FINRA and Commission staff.

[126] An investment adviser must register with the Commission unless it is prohibited from registering under Section 203A of the Investment Advisers Act of 1940 [15 U.S.C. 80b–3a] (the ''Advisers Act'') or is exempt from registration under Advisers Act Section 203 [15 U.S.C. 80b–3]. Investment advisers that are prohibited from registering with the Commission instead may be subject to regulation by the states, but the antifraud provisions of the

Continued

the Commission; and in the United States, attorneys and certified public accountants are licensed at the state level and are subject to rules of professional conduct [127] as well as, to the extent they appear or practice before the Commission in any way, to the Commission's Rules of Practice.[128]

We are including the fourth method in our non-exclusive list of methods that are deemed to satisfy the verification requirement in Rule 506(c) because we acknowledge that existing accredited investors who purchased securities in an issuer's Rule 506(b) offering prior to the effective date of Rule 506(c) would presumably participate in any subsequent offering by the same issuer conducted pursuant to Rule 506(c) based on their pre-existing relationships with the issuer. Accordingly, for these existing investors who were accredited investors in a Rule 506(b) offering prior to the effective date of Rule 506(c), a self-certification at the time of sale that he or she is an accredited investor will be deemed to satisfy the verification requirement in Rule 506(c). This provision does not extend to existing investors in an issuer who were not accredited investors in a Rule 506(b) offering that was conducted prior to the effective date of Rule 506(c).

While we have not adopted the recommendations of commenters who believe that even more prescriptive verification requirements are needed, we do recognize the general concern regarding possible misuse of the new Rule 506(c) exemption to sell securities to those who are not qualified to participate in the offering. We will closely monitor and study the development of verification practices by issuers, securities intermediaries and others by undertaking a review of whether such practices are, in fact, resulting in the exclusion of non-accredited investors from participation in these offerings, and the impact of compliance with this verification requirement on investor protection and capital formation.

C. Reasonable Belief That All Purchasers Are Accredited Investors

In the Proposing Release, we noted that a number of commenters had raised concerns that the language of Section 201(a) of the JOBS Act could be interpreted as precluding the use of the ''reasonable belief'' standard in the definition of ''accredited investor'' in Rule 501(a) in determining whether a purchaser is an accredited investor, such that an issuer's determination as to whether a purchaser is an accredited investor is subject to an absolute, rather than a ''reasonable belief,'' standard.[129] In their view, issuers may be more reluctant to use general solicitation in Rule 506 offerings if their determinations as to whether a purchaser is an accredited investor are subject to an absolute standard. Other commenters had interpreted the difference in the statutory language used in Section 201(a)(1) and Section 201(a)(2) [130] as indicating Congress' intent that the Commission ''raise the 'reasonable belief' standard for Rule 506 offerings . . . .'' [131]

Commenters on the Proposing Release were divided on the Commission's interpretation that the reasonable belief standard in Rule 501(a) applies to offerings under Rule 506(c). Several commenters supported this interpretation; [132] and other commenters opposed this interpretation.[133]

We are reaffirming the view that we expressed on this issue in the Proposing Release. In our view, the difference in the language between Section 201(a)(1) and Section 201(a)(2) reflects only the differing manner in which the reasonable belief standard was included in the respective rules at the time they were adopted, and does not represent a Congressional intent to eliminate the existing reasonable belief standard in Rule 501(a) or for Rule 506 offerings.[134] We note that the definition of accredited investor remains unchanged with the enactment of the JOBS Act and includes persons that come within any of the listed categories of accredited investors, as well as persons that the issuer reasonably believes come within any such category.

Further, as discussed in the Proposing Release, we continue to recognize that a person could provide false information or documentation to an issuer in order to purchase securities in an offering made under new Rule 506(c). Thus, even if an issuer has taken reasonable

Advisers Act continue to apply to them. *See* Advisers Act Sections 203A(b) and 206 [15 U.S.C. 80b–3(a), 15 U.S.C. 80b–6]. SEC-registered investment advisers are subject to examinations by Commission staff.

[127] Attorneys are subject to state standards for professional competence and ethical conduct, such as those based on the American Bar Association (''ABA'') Model Rules of Professional Conduct, which have been adopted by most states in the United States. For example, Rule 4.1 of the ABA Model Rules of Professional Conduct prohibits an attorney from knowingly making a false statement of material fact or law to a third person or failing to disclose a material fact to a third person when disclosure is necessary to avoid assisting a criminal or fraudulent act by a client. Accountants are also subject to state standards for professional competence and ethical conduct, such as those based on the AICPA Code of Professional Conduct. *See* AICPA Code of Professional Conduct ET 201.01, 202.01; *see also, e.g.,* The Uniform Accountancy Act (5th ed. 2007), available at: *http://www.aicpa.org/Advocacy/State/StateContactInfo/uaa/DownloadableDocuments/UAA_Fifth_Edition_January_2008.pdf.*

The Commission recognizes that there may be particular considerations a certified public accountant would need to take into account to comply with applicable professional standards for attestation engagements to provide a report that constitutes a confirmation in the context of this rule.

[128] *See* Rule 102(e) of the Rules of Practice [17 CFR 201.102(e)] (The Commission may censure a person or deny, temporarily or permanently, the privilege of appearing and practicing before it in any way to any person who is found by the Commission after notice and opportunity for hearing in the matter: (i) Not to possess the requisite qualifications to represent others; or (ii) To be lacking in character or integrity or to have engaged in unethical or improper professional conduct; or (iii) To have willfully violated, or willfully aided and abetted the violation of any provision of the Federal securities laws or the rules and regulations thereunder.).

[129] *See, e.g.,* letters from ABA Fed. Reg. Comm. (Apr. 30, 2012); BlackRock (May 3, 2012); NYCBA (May 4, 2012); W. Sjostrom, Jr. (Apr. 14, 2012).

[130] Section 201(a)(2) of the JOBS Act, which calls for amendments to Rule 144A, specifically refers to a ''reasonable belief'' standard as to whether a purchaser is a QIB, whereas Section 201(a)(1) does not mention a similar ''reasonable belief'' standard with respect to the amendments to Rule 506.

[131] Letter from Fund Democracy (May 24, 2012). *See also* letter from Massachusetts Securities Division (July 2, 2012).

[132] *See* letters from ABA Fed. Reg. Comm. (stating that it ''strongly support[s] the continued inclusion of the reasonable belief standard in the accredited investor definition, whether the offering is conducted under Rule 506(b) without general solicitation, or under Rule 506(c) with general solicitation''); IAA; MFA (Sept. 28, 2012) (stating that ''[e]liminating the 'reasonable belief' standard in the definition of accredited investor would preclude issuers from relying on Rule 506(c)'' and that, if this were the case, ''[i]ssuers would not engage in general solicitation and Section 201 would fail in its intended purposes to modernize the securities laws''); NSBA; NYCBA; P. Rutledge.

[133] *See* letters from AFL–CIO and AFR (stating that ''the legislative record reflects unmistakable congressional intent that securities sold through general solicitation and advertising under Rule 506 be sold only to accredited investors, not individuals issuers reasonably believe to be accredited investors''); Sen. Levin (stating that the ''Proposed Rule also creates, with no statutory basis, an alternative to the 'reasonable steps' requirement in the statute by stating that issuers may engage in a general solicitation or advertising so long as they 'reasonably believe' that the investors to be addressed will be accredited''); Consumer Federation (stating that a reasonable belief standard ''is in direct conflict with the statutory mandate that all investors in offerings sold through general solicitation and advertising be accredited investors and that the Commission specify methods issuers must follow to ensure that this is the case''); Fund Democracy (arguing that ''Congress intentionally chose not to make such [a reasonable belief] exception to the mandate that Rule 506 purchasers be accredited investors'').

[134] Both Rule 506 and Rule 144A currently provide for a reasonable belief standard regarding the eligibility of an investor to participate in an offering under the respective rules, but they reach that result in different ways. For Rule 506, the Commission chose to include the reasonable belief standard within the Rule 501(a) definition of ''accredited investor''; for Rule 144A, the Commission chose to include the standard as a condition, in paragraph (d)(1), to the use of the exemption.

steps to verify that a purchaser is an accredited investor, it is possible that a person nevertheless could circumvent those measures.[135] If a person who does not meet the criteria for any category of accredited investor purchases securities in a Rule 506(c) offering, we believe that the issuer will not lose the ability to rely on Rule 506(c) for that offering, so long as the issuer took reasonable steps to verify that the purchaser was an accredited investor and had a reasonable belief that such purchaser was an accredited investor at the time of sale.[136]

D. Form D Check Box for Rule 506(c) Offerings

Form D is the notice of an offering of securities conducted without registration under the Securities Act in reliance on Regulation D.[137] Under Rule 503 of Regulation D, an issuer offering or selling securities in reliance on Rule 504, 505 or 506 must file a notice of sales on Form D with the Commission for each new offering of securities no later than 15 calendar days after the first sale of securities in the offering. Form D is currently organized around 16 numbered ''items'' or categories of information. The information required to be provided in a Form D filing includes basic identifying information, such as the name of the issuer of the securities and the issuer's year and place of incorporation or organization; information about related persons (executive officers, directors, and promoters); the exemption or exemptions being claimed for the offering; and factual information about the offering, such as the duration of the offering, the type of securities offered and the total offering amount.

1. Proposed Form Amendment

We proposed revising Form D to add a separate field or check box for issuers to indicate whether they are claiming an exemption under Rule 506(c). Item 6 of Form D currently requires the issuer to identify the claimed exemption or exemptions for the offering from among Rule 504's paragraphs and subparagraphs, Rule 505, Rule 506 and former Section 4(5), as applicable. Under the proposal, a new check box in Item 6 of Form D would require issuers to indicate specifically whether they are relying on the Rule 506(c) exemption. In addition, the current check box for ''Rule 506'' would be renamed ''Rule 506(b),'' and the current check box for ''Section 4(5)'' would be renamed ''Section 4(a)(5)'' to update the reference to former Section 4(5) of the Securities Act.

We explained in the Proposing Release that this revision would provide additional information needed to assist our efforts to analyze the use of general solicitation in Rule 506(c) offerings and the size of this offering market. The information would also help us to look into the practices that may develop to satisfy the verification requirement, which would assist us in assessing the effectiveness of various verification practices in identifying and excluding non-accredited investors from participation in Rule 506(c) offerings.

2. Comments on the Proposed Form Amendment

Most commenters who expressed a view on the proposed checkbox in Form D supported the addition of this checkbox for issuers to indicate whether they are relying on Rule 506(c) for their offerings.[138] Only one commenter opposed the proposed checkbox.[139] A number of commenters recommended that the Commission include additional information requirements in Form D for Rule 506(c) offerings, beyond a checkbox to indicate reliance on Rule 506(c).[140] Some commenters asked for confirmation that issuers may check *both* the Rule 506(b) box and the Rule 506(c) box in a Form D under certain circumstances.[141]

3. Final Form Amendment

We are adopting the revision to Form D as proposed. Issuers conducting Rule 506(c) offerings must indicate that they are relying on the Rule 506(c) exemption by marking the new check box in Item 6 of Form D. Further, as proposed, the current check box for ''Rule 506'' will be renamed ''Rule 506(b),'' and the current check box for ''Section 4(5)'' will be renamed ''Section 4(a)(5).''

We are of the view that an issuer will not be permitted to check both boxes at the same time for the same offering. We remind issuers that once a general solicitation has been made to the purchasers in the offering,[142] an issuer is precluded from making a claim of reliance on Rule 506(b), which remains subject to the prohibition against general solicitation, for that same offering.

E. Specific Issues for Private Funds

Private funds, such as hedge funds, venture capital funds and private equity funds, typically rely on Section 4(a)(2) and Rule 506 to offer and sell their interests without registration under the Securities Act.[143] In addition, private funds generally rely on one of two exclusions from the definition of ''investment company'' under the Investment Company Act—Section

[135] We note that several federal courts have been unsympathetic to attempts by investors who represented that they were accredited investors at the time of the sale of securities to subsequently disavow those representations in order to pursue a cause of action under the federal securities laws. *See, e.g., Wright* v. *Nat'l Warranty Co.,* 953 F.2d 256 (6th Cir. 1991) (rejecting the plaintiffs' argument that Rule 505 was unavailable because the plaintiffs ''specifically warranted and represented in the subscription agreement . . . that they were accredited investors''); *Goodwin Properties, LLC* v. *Acadia Group, Inc.,* No. 01–49–P–C, 2001 U.S. Dist. LEXIS 9975 (D. Me. 2001) (noting that the plaintiffs ''provided the defendants with reason to believe that they were accredited investors as defined by 17 C.F.R. § 230.501(a)'' and stating that therefore ''[t]hey cannot now disavow those representations in order to support their claims against the defendants''); *Faye L. Roth Revocable Trust* v. *UBS Painewebber Inc.,* 323 F. Supp. 2d 1279 (S.D. Fla. 2004) (stating that the plaintiffs ''cannot disavow their representations that they were accredited investors'' and concluding that there was no material dispute that the offering complied with Regulation D).

[136] Our views regarding an issuer's ability to maintain the exemption for a Rule 506(c) offering notwithstanding the fact that not all purchasers meet the criteria for any category of accredited investor are consistent with our views regarding the effect of attempts by prospective investors to circumvent the requirement in Regulation S that offers and sales be made only to non-U.S. persons. *See Statement of the Commission Regarding Use of Internet Web sites to Offer Securities, Solicit Securities Transactions or Advertise Investment Services Offshore,* Release No. 33–7516 (Mar. 23, 1998) [63 FR 14806 (Mar. 27, 1998)] (''In our view, if a U.S. person purchases securities or investment services notwithstanding adequate procedures reasonably designed to prevent the purchase, we would not view the Internet offer after the fact as having been targeted at the United States, absent indications that would put the issuer on notice that the purchaser was a U.S. person.'').

[137] Form D also applies to offerings conducted using the Section 4(a)(5) exemption. The Commission adopted Form D when it adopted Regulation D in 1982. Release No. 33–6389 (adopting Form D as a replacement for Forms 4(6), 146, 240 and 242).

[138] *See, e.g.,* letters from MFA (Sept. 28, 2012); BIO; S&C; Tannenbaum Helpern; ABA Fed. Reg. Comm.; IAA; SIFMA and FSR (Oct. 5, 2012); SRC of NYSBA.

[139] Letter from J. McLaughlin (stating that ''Section 201(a)(1) does not authorize the Commission to impose a separate Form D filing requirement on issuers who choose to engage in general solicitation'').

[140] *See, e.g.,* letters from AARP; AFL–CIO and AFR; Consumer Federation; Investor Advisory Committee; NASAA; Massachusetts Securities Division (July 2, 2012); Fund Democracy.

[141] *See* letters from J. Gross; NYCBA; IAA.

[142] That is, the purchasers became interested in the offering because of, or through, the general solicitation, and not through some means other than the general solicitation, such as through a substantive, pre-existing relationship with the company or direct contact by the company or its agents outside of the general solicitation. *See Revisions of Limited Offering Exemptions in Regulation D,* Release No. 33–8828 (Aug. 3, 2007) [72 FR 45116, 45129 (Aug. 10, 2007)].

[143] *See, e.g., Implications of the Growth of Hedge Funds, Staff Report to the Securities and Exchange Commission* (Sept. 2003) (''Staff Report on Hedge Funds''), available at: *http://www.sec.gov/news/studies/hedgefunds0903.pdf.*

3(c)(1) [144] and Section 3(c)(7) [145]—which enables them to be excluded from substantially all of the regulatory provisions of that Act.[146] Private funds are precluded from relying on either of these two exclusions if they make a public offering of their securities.[147] Section 3(c)(1) excludes from the definition of ''investment company'' any issuer whose outstanding securities (other than short-term paper) are beneficially owned by not more than 100 beneficial owners,[148] and which is not making and does not presently propose to make a public offering of its securities. Section 3(c)(7) excludes from the definition of ''investment company'' any issuer whose outstanding securities are owned exclusively by persons who, at the time of acquisition of such securities, are ''qualified purchasers,'' [149] and which is not making and does not at that time propose to make a public offering of its securities.

Section 201(a)(1) of the JOBS Act directs the Commission to eliminate the prohibition against general solicitation for a new category of Rule 506 offerings, and makes no specific reference to private funds. Section 201(b) of the JOBS Act also provides that ''[o]ffers and sales exempt under [Rule 506, as revised pursuant to Section 201(a)] shall not be deemed public offerings under the Federal securities laws as a result of general advertising or general solicitation.'' We historically have regarded Rule 506 transactions as non-public offerings for purposes of Sections 3(c)(1) and 3(c)(7).[150] As we stated in the Proposing Release and reaffirm here, the effect of Section 201(b) is to permit private funds to engage in general solicitation in compliance with new Rule 506(c) without losing either of the exclusions under the Investment Company Act.

A few commenters argued that Section 201(b) does not permit private funds to engage in general solicitation under proposed Rule 506(c) without losing their exclusions under the Investment Company Act.[151] In our view, although Section 201(b) does not explicitly reference the meaning of ''public offering'' under the Investment Company Act, it clearly states that ''[o]ffers and sales exempt under [Rule 506, as revised pursuant to Section 201(a)] shall not be deemed public offerings under the *Federal securities laws* as a result of general advertising or general solicitation'' (emphasis added). As the Investment Company Act is a federal securities law, the effect of Section 201(b) is to permit offers and sales of securities under Rule 506(c) by private funds relying on the exclusions from the definition of ''investment company'' under Section 3(c)(1) or Section 3(c)(7) of the Investment Company Act.

Some commenters expressed concerns about private funds engaging in general solicitation under proposed Rule 506(c).[152] Other commenters, however, supported the removal of the prohibition against general solicitation in Rule 506(c) offerings with respect to private funds,[153] with some commenters stating that the removal of the ban would bring greater transparency to the private fund industry and allow managers of private funds to communicate more effectively with the public and prospective investors.[154]

Some commenters who were concerned about private funds engaging in general solicitation recommended that we impose additional conditions on private funds that rely on Rule 506(c). In particular, a number of commenters believed that private funds engaging in general solicitation should be subject to some form of content and/or other restrictions, and suggested potential methods.[155] For example, some believed that, in order to engage in general solicitation, private funds should be held to performance and advertising standards that are analogous to mutual fund standards.[156] One of these commenters suggested that the Commission develop rules tailored to the ways private funds calculate and present investment performance, rather than extending mutual fund performance rules to private funds.[157] Some made other suggestions, such as

[144] 15 U.S.C. 80a–3(c)(1).

[145] 15 U.S.C. 80a–3(c)(7).

[146] We also refer in this release to ''pooled investment funds'' because that term is used in Form D. Issuers that rely on Section 3(c)(1) or 3(c)(7) of the Investment Company Act are a subset of pooled investment funds.

[147] *See also* Section 202(a)(29) of the Advisers Act [15 U.S.C. 80b–2(a)(29)] (defining a ''private fund'' as an issuer that would be an investment company under the Investment Company Act, but for Sections 3(c)(1) or 3(c)(7) of that Act). Many ABS issuers also rely on the exclusions contained in Sections 3(c)(1) or 3(c)(7) of the Investment Company Act. These ABS issuers frequently participate in Rule 144A offerings.

[148] *See also* Rule 3c–5 under the Investment Company Act [17 CFR 270.3c–5] (providing that the section's limit of 100 beneficial owners does not include ''knowledgeable employees,'' as defined in the rule).

[149] *See* Section 2(a)(51) of the Investment Company Act [15 U.S.C. 80a–2(a)(51)] and the rules there under. *See Also* Rule 3c–5 under the Investment Company Act (excluding ''knowledgeable employees'' from the determination of whether all of the outstanding securities of the fund relying on Section 3(c)(7) are owned exclusively by qualified purchasers).

[150] *See* Release No. 33–6389 (noting that the ''Commission regards rule 506 transactions as non-public offerings for purposes of the definition of 'investment company' in section 3(c)(1) of the Investment Company Act''); *Privately Offered Investment Companies,* Release No. IC–22597 (Apr. 3, 1997) [62 FR 17512 (Apr. 9, 1997)], at n. 5 (noting that the ''Commission believes that section 3(c)(7)'s public offering limitation should be interpreted in the same manner as the limitation in section 3(c)(1)'').

[151] *See* letter from Fund Democracy (stating that ''Section 201(b) refers only to Rule 506; it makes no reference to the meaning of 'public offering' under the Investment Company Act exemptions''). *See also* letter from AFL–CIO and AFR.

[152] *See, e.g.,* letters from A. La Rosa; A. Pierwola; AFL–CIO and AFR; C. Erickson; Consumer Federation; E. Guthrie; F. Urling; Fund Democracy; J. Clark; K. Pesson; M. Gessford; M. Trail; M. Zartler; R. Dunn; S. Johnston; W. Cunningham.

[153] *See, e.g.,* letters from BlackRock; Dukas; Forum for U.S. Securities Lawyers in London; HFA; IAA; MFA (Sept. 28, 2012); NYCBA; SRC of NYSBA.

[154] *See, e.g.,* letters from Dukas; HFA.

[155] *See, e.g.,* letters from ICI; AFL–CIO and AFR; C. Corn; Sen. Levin (stating that ''Congress did not contemplate removing the general solicitation ban—without retaining any limitations on forms of solicitation—for private investment vehicles''); Consumer Federation; D. Kronheim; D. Smith; Fund Democracy; G. Lavy; G. Morin; Investor Advisory Committee; IDC; J. Sanders; Rep. Waters; NASAA; P. Turney; Sens. Reed, Levin, Durbin, Harkin, Lautenberg, Franken and Akaka.

[156] *See, e.g.,* letters from C. Corn; Sen. Levin (noting that ''[a]lready, the Commission has determined that the manner and substance of solicitation and advertising for investments in registered investment companies deserves significant regulatory oversight. Many of those same concerns apply to investments in private investment vehicles. Accordingly, the Commission should impose analogous protections for investments in private funds.''); Consumer Federation (stating that ''[s]hort of an outright prohibition on general solicitation and advertising by private funds, the Commission should at the very least adopt clear standards for the reporting of performance and fees by private funds, and delay their eligibility from engaging in general solicitation and advertising until such time as those standards are in place,'' including a requirement to include in private fund advertisements ''a clear, prominent warning that they are not mutual funds and carry special risks.''); D. Kronheim; D. Smith; Fund Democracy (noting that an alternative would be to ''apply mutual fund advertising and valuation rules to hedge funds that engage in [general solicitation and advertising] (and, in any case, require standardized performance and fee reporting for all hedge funds), and require explicit, large-font disclaimers that hedge funds are not mutual funds and present special risks.''); G. Lavy; ICI (recommending content restrictions on private fund advertising at least as extensive as those currently applicable to mutual funds (*e.g.,* disclaimers regarding the performance figures or measures displayed in any advertisement), with a prohibition on use of performance advertising until the Commission can develop a new rule regarding such advertising); IDC; NASAA (stating that ''because the investment strategies of private funds are typically more opaque, risky, and illiquid than those of mutual funds, private fund advertisements should be subject to restrictions that are comparable to the rules for mutual funds.''); P. Turney.

[157] *See* letter from ICI (arguing that the antifraud provisions in Section 206(4) of the Advisers Act [15 U.S.C. 80b–6(4)] and Rule 206(4)–8 thereunder [17 CFR 275.206(4)–8] would not be enough to protect investors because these advertisements will be presented before accredited and non-accredited investors at the same time).

requiring each private fund relying on Rule 506(c) to disclose that the private fund is not registered with the Commission and should not be confused with a registered fund, such as a mutual fund.[158] With respect to private funds sold through broker-dealers subject to FINRA's rules of conduct, some commenters believed that we should direct FINRA to require the filing and review of private fund advertisements.[159]

Finally, some commenters opposed the imposition of content and/or other restrictions for private funds.[160] They asserted that purchasers of the securities of a private fund that relies on Rule 506(c), must be, at a minimum, accredited investors and thus have met objective criteria demonstrating financial sophistication, which they believed eliminates the risk that other types of investors could be defrauded.[161] A number of commenters pointed out that advertisements of private funds are subject to the antifraud provisions of the federal securities laws and suggested that liability under such provisions provides sufficient investor protections.[162]

We have carefully considered commenters' suggestions and concerns. We are mindful of certain commenters' concerns that private funds engaging in general solicitation may raise certain investor protection issues. We also understand that other commenters believe that additional measures regarding private fund advertising are not necessary because the antifraud provisions of the federal securities laws continue to apply. We will monitor and study the development of private fund advertising and undertake a review to determine whether any further action is necessary.

We remind investment advisers to private funds that they are subject to Rule 206(4)–8 under the Advisers Act.[163] Rule 206(4)–8 provides that it shall constitute a fraudulent, deceptive or manipulative act, practice or course of business within the meaning of Section 206(4) of the Advisers Act for any investment adviser to a pooled investment vehicle[164] to ''(1) [m]ake any untrue statement of a material fact or to omit to state a material fact necessary to make the statements made, in light of the circumstances under which they were made, not misleading, to any investor or prospective investor in the pooled investment vehicle; or (2) otherwise engage in any act, practice or course of business that is fraudulent, deceptive, or manipulative with respect to any investor or prospective investor in the pooled investment vehicle.''[165]

As was stated by the Commission when it adopted Rule 206–4(8), ''[t]he rule clarifies that an adviser's duty to refrain from fraudulent conduct under the federal securities laws extends to the relationship with ultimate investors and that the Commission may bring enforcement actions under the Advisers Act against investment advisers who defraud investors or prospective investors in those pooled investment vehicles.''[166] We further stated that we ''intend to employ all of the broad authority that Congress provided us in section 206(4) and direct it at adviser conduct affecting an investor or potential investor in a pooled investment vehicle.''[167] Recently, for example, we have brought enforcement actions against private fund advisers and others for material misrepresentations to investors and prospective investors regarding fund performance, strategy, and investments, among other things.[168]

We believe that investment advisers that have implemented appropriate policies and procedures regarding, among other things, the nature and content of private fund sales literature, including general solicitation materials, are less likely to use materials that materially mislead investors or otherwise violate the federal securities laws. Accordingly, we believe that investment advisers to private funds should carefully review any such policies and procedures that have been implemented to determine whether they are reasonably designed to prevent the use of fraudulent or materially misleading private fund advertising and make appropriate amendments to those policies and procedures, particularly if the private funds intend to engage in general solicitation activity.[169]

F. Technical and Conforming Amendments

We proposed a number of technical and conforming amendments to Rules 502 and 506 of Regulation D. Under the proposal, we would amend various provisions in Rule 502(b) to clarify that the references to sales to non-accredited investors under Rule 506, and the corresponding informational requirements, would be applicable to offerings under Rule 506(b) and not to offerings under Rule 506(c). We proposed to amend Rule 502(c) to clarify that Rule 502(c)'s prohibition against general solicitation would not apply to offerings under Rule 506(c). In addition, as Section 201(c) of the JOBS Act renumbered Section 4 of the Securities Act, we proposed to amend Regulation D and Rule 144A to update the references to Section 4. Finally, the proposal would update references to Section 2 of the Securities Act in these rules as some of the references have not been updated to reflect the current numbering scheme in Section 2. We received no comments regarding these technical and conforming amendments and are adopting these rule amendments as proposed.

[158] *See* letters from ICI; IDC.

[159] *See* letters from AFL–CIO and AFR (stating that ''FINRA already pre-reviews broker-dealer advertising; the same requirement should apply to general solicitation and advertising in Rule 506 offerings in light of the significant potential for abuse.''); ICI (noting that ''FINRA has developed an infrastructure to handle such filings and an expertise to substantively review them, and accordingly is best positioned to handle this task.'').

[160] *See, e.g.,* letters from Verrill Dana LLP (stating that ''[t]here is no suggestion in Section 201 that the Commission must distinguish between 'issuers that engage in operational businesses' and 'those that are merely investment vehicles'''); Artivest (noting that for private funds managed by a registered commodity pool operator, the National Futures Association Rule 2–29 contains standards regarding marketing materials).

[161] In general, private funds that pay performance fees to their managers are available only to ''qualified clients'' that have at least $1 million in assets under management or that have a net worth of $2 million (excluding the value of the client's primary residence). *See* Rule 205–3 under the Advisers Act [17 CFR 275.205–3]. *See also* letter from BlackRock.

[162] *See, e.g.,* letters from BlackRock; HFA; MFA (Mar. 22, 2013).

[163] 17 CFR 275.206(4)–8.

[164] Rule 206(4)–8 defines a pooled investment vehicle to mean any investment company as defined in Section 3(a) of the Investment Company Act [15 U.S.C. 80a–3(a)] or any company that would be an investment company under Section 3(a) of that Act but for the exclusion provided from that definition by either Section 3(c)(1) or Section 3(c)(7) of that Act [15 U.S.C. 80a–3(c)(1) or (7)].

[165] *Id.*

[166] *Prohibition of Fraud by Advisers to Certain Pooled Investment Vehicles,* Release No. IA–2628 (Aug. 3, 2007) [72 FR 44756 (Aug. 9, 2007)].

[167] *Id.*

[168] *See, e.g., In the Matter of Oppenheimer Asset Management Inc. and Oppenheimer Alternative Investment Management, LLC,* Release No. IA–3566 (Mar. 11, 2013); *In the Matter of Sentinel Investment Management Corp.,* Release No. IA–3530 (Dec. 27, 2012); *In the Matter of Weizhan Tang,* Release No. IA–3482 (Oct. 5, 2012); *In the Matter of Calhoun Asset Management, LLC, et al.,* Release No. IA–3428 (July 9, 2012); *In the Matter of Belal K. Faruki,* Release No. IA–3405 (May 17, 2012); *In the Matter of GMB Capital Management LLC, et al.,* Release No. IA–3399 (Apr. 20, 2012).

[169] We remind investment advisers that are registered or required to be registered under Section 203 of the Advisers Act that they must adopt and implement written policies and procedures reasonably designed to prevent violations of the Advisers Act which include, but are not limited to, violations of Section 206 of the Advisers Act and the rules thereunder. They must also review, no less frequently than annually, the adequacy of the written policies and procedures and the effectiveness of the policies and procedures' implementation. *See* CFR 275.206(4)–7.

III. Final Amendment to Rule 144A

Section 201(a)(2) of the JOBS Act directs the Commission to revise Rule 144A(d)(1) under the Securities Act to provide that securities sold pursuant to Rule 144A may be offered to persons other than QIBs, including by means of general solicitation, provided that securities are sold only to persons that the seller and any person acting on behalf of the seller reasonably believe is a QIB. To implement the mandated rule change, we proposed amending Rule 144A(d)(1) to eliminate the references to ''offer'' and ''offeree.'' All of the commenters that expressed a view on the proposed amendment to Rule 144A(d)(1) stated that they supported the Commission's proposal.[170] We are adopting the amendment as proposed. As amended, Rule 144A(d)(1) will require only that the securities be sold to a QIB or to a purchaser that the seller and any person acting on behalf of the seller reasonably believe is a QIB.[171] Under this amendment, resales of securities pursuant to Rule 144A can be conducted using general solicitation, so long as the purchasers are limited in this manner.[172]

As a result of the Section 201(a)(2) mandate and the resulting Rule 144A revisions, we are also making technical and conforming revisions to the exceptions in Regulation M relating to transactions in Rule 144A securities, specifically Regulation M Rules 101(b)(10), 102(b)(7) and 104(j)(2). When adopted in 1996, the exceptions delineated in Rules 101(b)(10)(i), 102(b)(7)(i) and 104(j)(2)(i) were generally intended to permit transactions in securities eligible for resale under Rule 144A during a distribution of securities, provided that offers and sales of such securities were made solely to QIBs or persons reasonably believed to be QIBs in certain transactions exempt from registration.[173]

As explained above, Section 201(a)(2) of the JOBS Act directs the Commission to revise Rule 144A to permit offers of securities to persons other than QIBs. As noted above, Rule 144A is being amended to eliminate references to ''offer'' and ''offeree,'' so that the amended rule will require only that securities be sold to a QIB or to a purchaser that the seller and any person acting on behalf of the seller reasonably believes is a QIB.

In order to conform the language in Regulation M to Rule 144A, as amended, we are conforming the Regulation M exceptions by similarly eliminating the references to ''offered'' and ''offerees.'' We believe that these conforming modifications do not result in any substantive change to the Regulation M exceptions and are consistent with the purpose of the exceptions.

As a transition matter, for an ongoing Rule 144A offering that commenced before the effective date of the amendment to Rule 144A(d)(1), offering participants will be entitled to conduct the portion of the offering following the effective date of the amendment to Rule 144A(d)(1) using general solicitation, without affecting the availability of Rule 144A for the portion of the offering that occurred prior to the effective date of the amended rule.

IV. Integration With Offshore Offerings

In the Proposing Release, we noted that the mandate in Section 201(a) that the Commission amend Rule 506 and Rule 144A to permit the use of general solicitation in transactions under those rules has raised questions from some commenters[174] regarding the impact of the use of general solicitation on the availability of the Regulation S safe harbors for concurrent unregistered offerings inside and outside the United States.[175] The safe harbors are important when U.S. and non-U.S. companies engage in global offerings of securities in which the U.S. portion of the offering is conducted in accordance with Rule 144A or Rule 506 and the offshore portion is conducted in reliance on Regulation S.

We expressed our view on this issue in the Proposing Release, which we are reaffirming in this release.[176] Concurrent offshore offerings that are conducted in compliance with Regulation S will not be integrated with domestic unregistered offerings that are conducted in compliance with Rule 506 or Rule 144A, as amended. As explained in the Proposing Release, we believe that our view is consistent with the historical treatment of concurrent Regulation S and Rule 144A/Rule 506 offerings.[177]

V. Paperwork Reduction Act

A. Background

The amendment to Form D contains a ''collection of information'' requirement within the meaning of the Paperwork Reduction Act of 1995 (''PRA'').[178] We published a notice requesting comment on the collection of information requirement in the Proposing Release for the rule and form amendments. We submitted that requirement to the Office of Management and Budget (''OMB'') for review and approval in accordance with the PRA and its implementing regulations.[179] The title of this requirement is: ''Form D'' (OMB Control No. 3235–0076).[180]

We adopted Regulation D and Form D as part of the establishment of a series

[170] *See* letters from IAA; SIFMA and FSR (Oct. 5, 2012); J. Johnson; OTC Markets Group Inc.

[171] Rule 144A(d)(1).

[172] The general solicitation that is permitted in Rule 144A resales from the initial purchaser to the QIBs will not affect the availability of the Section 4(a)(2) exemption or Regulation S for the initial sale of securities by the issuer to the initial purchaser.

[173] *See Anti-Manipulation Rules Concerning Securities Offerings,* Release No. 34–38067 (Dec. 20, 1996) [62 FR 520 (Jan. 3, 1997)] at 530 (''As adopted, the exception permits transactions in Rule 144A Securities during a distribution of such securities, provided that sales of such securities within the United States are made solely to: Qualified institution buyers ('QIBs'), or persons reasonably believed to be QIBs, in transactions exempt from registration under the Securities Act . . . The exception covers both the Rule 144A security being distributed and any reference security.'').

[174] *See, e.g.,* letters from ABA Fed. Reg. Comm. (Apr. 30, 2012); L. Neumann (June 12, 2012); NYCBA (May 4, 2012); SecuritiesLawUSA, PC (June 26, 2012); SIFMA (Apr. 27, 2012).

[175] Regulation S provides a safe harbor for offers and sales of securities outside the United States and includes an issuer and a resale safe harbor. Two general conditions apply to both safe harbors: (1) The securities must be sold in an offshore transaction and (2) there can be no ''directed selling efforts'' in the United States. Rule 902(c)(1) [17 CFR 230.902(c)(1)] broadly defines ''directed selling efforts'' as: Any activity undertaken for the purpose of, or that could reasonably be expected to have the effect of, conditioning the market in the United States for any of the securities offered in reliance on Regulation S. Such activity includes placing an advertisement in a publication ''with a general circulation in the United States'' that refers to the offering of securities being made in reliance upon Regulation S.

[176] All of the commenters who expressed a view on our interpretation supported it and encouraged us to reiterate it in this release. *See* letters from ABA Fed. Reg. Comm; Forum for U.S. Securities Lawyers in London; IAA; IPA; NYCBA.

[177] *See Offshore Offers and Sales,* Release No. 33–6863 (Apr. 24, 1990) [55 FR 18306 (May 2, 1990)] (stating that ''[o]ffshore transactions made in compliance with Regulation S will not be integrated with registered domestic offerings or domestic offerings that satisfy the requirements for an exemption from registration under the Securities Act.''). In addressing the offshore transaction component of the Regulation S safe harbor, the Commission also stated, ''Offers made in the United States in connection with contemporaneous registered offerings or offerings exempt from registration will not preclude reliance on the safe harbors.'' *Id.* at n. 36. Likewise, in addressing directed selling efforts, the Commission stated, ''Offering activities in contemporaneous registered offerings or offerings exempt from registration will not preclude reliance on the safe harbors.'' *Id.* at n. 47. *See also* Rule 500(g) of Regulation D [17 CFR 230.500(g)] (formerly Preliminary Note No. 7 to Regulation D) (''Regulation S may be relied upon for such offers and sales even if coincident offers and sales are made in accordance with Regulation D inside the United States.'').

[178] 44 U.S.C. 3501 *et seq.*

[179] 44 U.S.C. 3507(d); 5 CFR 1320.11.

[180] Form D was adopted under the authority of Sections 2(a)(15), 3(b), 4(a)(2), 19(a) and 19(c)(3) of the Securities Act [15 U.S.C. 77b(a)(15), 77c(b), 77d(a)(2), 77s(a) and 77s(c)(3)].

of exemptions for offerings and sales of securities under the Securities Act. The Form D filing is required to be made by issuers as a notice of sales without registration under the Securities Act based on a claim of exemption under Regulation D or Section 4(a)(5) of the Securities Act. The Form D filing is required to include basic information about the issuer, certain related persons, and the offering. This information is needed for implementing the exemptions and analyzing their use. The information collection requirements related to the filing of Form D with the Commission are mandatory to the extent that an issuer elects to make an offering of securities in reliance on the relevant exemption. Responses are not confidential. The hours and costs associated with preparing and filing forms and retaining records constitute reporting and cost burdens imposed by the collection of information requirements. An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information requirement unless it displays a currently valid OMB control number.

As discussed above, we proposed to amend Form D to add a check box to indicate an offering relying on the Rule 506(c) exemption. In the Proposing Release, we requested comment on our PRA burden hour and cost estimates and the analysis used to derive such estimates. One commenter responded to our request for comment on the PRA analysis and stated that it believed that the cost estimates in the PRA and economic analysis are too low.[181]

B. Revisions to PRA Reporting and Cost Burden Estimates

Consistent with the PRA analysis in the Proposing Release, we believe that the addition of a check box on Form D to indicate that an issuer is relying on the Rule 506(c) exemption for its offering will have a negligible effect on the paperwork burden of the form. Form D already contains a check box for each basis of exemption claimed under Regulation D; this change simply conforms the form to the new rule amendment. Accordingly, we estimate that under the amendment to Form D, the burden for responding to the collection of information in Form D will be substantially the same as before the amendment to Form D. We believe, however, that the amendment to Rule 506 could increase the number of Form D filings that are made with the Commission because we expect issuers may conduct more Rule 506 offerings.

The table below shows the current total annual compliance burden, in hours and in costs, of the collection of information pursuant to Form D. For purposes of the PRA, we estimate that, over a three-year period, the average burden estimate will be four hours per Form D filing. Our burden estimate represents the average burden for all issuers. This burden is reflected as a one hour burden of preparation on the issuer and a cost of $1,200 per filing. In deriving these estimates, we assume that 25% of the burden of preparation is carried by the issuer internally and that 75% of the burden of preparation is carried by outside professionals retained by the issuer at an average cost of $400 per hour. The portion of the burden carried by outside professionals is reflected as a cost, while the portion of the burden carried by the issuer internally is reflected in hours.

TABLE 1—ESTIMATED PAPERWORK BURDEN UNDER FORM D, PRE-AMENDMENT TO RULE 506

	Number of responses (A)[182]	Burden hours/form (B)	Total burden hours (C)=(A)*(B)	Internal issuer time (D)	External professional time (E)	Professional costs (F)=(E)*$400
Form D	18,187	4	72,748	18,187	54,561	$21,824,400

According to our Division of Economic and Risk Analysis (''DERA''), in 2012, 16,067 companies made 18,187 new Form D filings. The annual number of new Form D filings rose from 13,764 in 2009 to 18,187 in 2012, an average increase of approximately 1,474 Form D filings per year, or approximately 10%. Assuming that the macroeconomic factors underlying this increase persist and the number of Form D filings continues to increase by 1,474 filings per year for each of the next three years, the average number of Form D filings in each of the next three years, absent the elimination of the prohibition against general solicitation, would be approximately 21,135.

We anticipate that new paragraph (c) of Rule 506 could result in an even greater annual increase in the number of Form D filings than the 10% annual increase estimated above. As a reference point for the potential increase, we use the impact of another past rule change on the market for Regulation D offerings. In 1997, the Commission amended Rule 144(d) under the Securities Act[183] to reduce the holding period for restricted securities from two years to one year,[184] thereby increasing the attractiveness of Regulation D offerings to investors and to issuers. There were 10,341 Form D filings in 1996. This was followed by a 20% increase in the number of Form D filings in each of the subsequent three calendar years, reaching 17,830 by 1999. Although it is not possible to predict with any degree of accuracy the increase in the number of Rule 506 offerings following the elimination of the prohibition against general solicitation for a new category of Rule 506 offerings, we assume for purposes of this analysis that there could be a similarly significant increase.

For purposes of the PRA and based on our analysis above, we estimate that the amendment to Rule 506 will result in a 20% increase in Form D filings relying on the Rule 506 exemption, or approximately 3,637 filings.[185] We also assume that the number of Form D filings will increase by approximately 3,637 in each year following the adoption of the rule.

[181] *See* letter from NSBA (stating that ''the compliance cost estimates should include the time required by the issuer and their advisors to familiarize themselves with the rule and to comply with the additional verification requirements and the time and costs of investors to comply (for example, with a third-party verification requirement)''). For PRA purposes, we consider only the burden of responding to the collection of information in Form D; we do not consider any of the other costs, direct or indirect, of conducting a Rule 506(c) offering.

[182] We had previously estimated the number of responses to be 25,000, as reflected in OMB's Inventory of Currently Approved Information Collections (available at: *http://www.reginfo.gov/public/do/PRAMain;jsessionid=D37174B5F6F9148DB767D63DF6983A65*), but we are revising this estimate to reflect the number of new Form D filings made in 2012.

[183] 17 CFR 230.144(d).

[184] *See Revision of Holding Period Requirements in Rules 144 and 145,* Release No. 33–7390 (Feb. 20, 1997) [62 FR 9242 (Feb. 28, 1997)].

[185] This number is based on the 18,187 new Form D filings that were made in 2012.

Based on this increase, we estimate that the annual compliance burden of the collection of information requirements for the first year in which issuers will make Form D filings after the adoption of Rule 506(c) will be an aggregate of 21,824 hours of issuer personnel time and $26,188,800 for the services of outside professionals per year.

TABLE 2—ESTIMATED PAPERWORK BURDEN UNDER FORM D, POST-AMENDMENT TO RULE 506

	Number of responses (A) [186]	Burden hours/form (B)	Total burden hours (C)=(A)*(B)	Internal issuer time (D)	External professional time (E)	Professional costs (F)=(E)*$400
Form D	21,824	4	87,296	21,824	65,472	$26,188,800

VI. Economic Analysis

A. Background

We are adopting amendments to Rule 506 and Rule 144A to implement the requirements of Section 201(a) of the JOBS Act.[187] Section 201(a)(1) directs the Commission to revise Rule 506 to provide that the prohibition against general solicitation contained in Rule 502(c) shall not apply to offers and sales of securities made pursuant to Rule 506, as amended, provided that all purchasers of the securities are accredited investors. Section 201(a)(1) also provides that ''such rules shall require the issuer to take reasonable steps to verify that purchasers of the securities are accredited investors, using such methods as determined by the Commission.'' Section 201(a)(2) of the JOBS Act directs the Commission to revise Rule 144A(d)(1) to provide that securities sold pursuant to Rule 144A may be offered to persons other than QIBs, including by means of general solicitation, provided that securities are sold only to persons that the seller and any person acting on behalf of the seller reasonably believe are QIBs.

We are mindful of the costs imposed by and the benefits obtained from our rules. The discussion below addresses the economic effects of the amendments to Rule 506, Rule 144A and Form D, including the likely benefits and costs of the amendments as well as the effect of the amendments on efficiency, competition and capital formation.[188] Some of the costs and benefits stem from the statutory mandate of Section 201(a), whereas others are affected by the discretion we have exercised in implementing this mandate. These two types of costs and benefits may not be entirely separable to the extent that our discretion is exercised to realize the benefits that we believe were intended by Section 201(a).

B. Economic Baseline

The baseline analysis that follows is in large part based on information collected from Form D filings submitted by issuers relying on Regulation D to raise capital. As we describe in more detail below, we believe that we do not have a complete view of the Rule 506 market, particularly with respect to the amount of capital raised. Currently, issuers are required to file a Form D within 15 days of the first sale of securities, and are required to report additional sales through amended filings only under certain conditions. In addition, issuers may not report all required information, either due to error or because they do not wish to make the information public. Commenters have suggested and we also have evidence that some issuers do not file a Form D for their offerings in compliance with Rule 503.[189] Consequently, the analysis that follows is necessarily subject to these limitations in the current Form D reporting process.

1. Size of the Exempt Offering Market

Exempt offerings play a significant role in capital formation in the United States. Offerings conducted in reliance on Rule 506 account for 99% of the capital reported as being raised under Regulation D from 2009 to 2012, and represent approximately 94% of the number of Regulation D offerings.[190] The significance of Rule 506 offerings is underscored by the comparison to registered offerings. In 2012, the estimated amount of capital reported as being raised in Rule 506 offerings (including both equity and debt) was $898 billion, compared to $1.2 trillion raised in registered offerings.[191] Of this $898 billion, operating companies (issuers that are not pooled investment funds) reported raising $173 billion, while pooled investment funds reported raising $725 billion.[192] The amount reported as being raised by pooled investment funds is comparable to the amount of capital raised by registered investment funds. In 2012, registered investment funds (which include money market mutual funds, long-term mutual funds, exchange-traded funds, closed-end funds and unit investment trusts) raised approximately $727 billion.[193]

[186] The information in this column is based on the 18,187 new Form D filings that were made in 2012, plus the additional 3,637 filings we estimate would be filed in the first year after the effectiveness of Rule 506(c).

[187] As explained above, the Commission in this release is adopting only those rule and form amendments that are specifically mandated by Section 201(a). Correspondingly, we analyze the economic impacts—including the benefits and costs—only of those rules and form amendments considered within the scope of this release.

[188] Section 2(b) of the Securities Act [15 U.S.C. 77b(b)] requires the Commission, when engaging in rulemaking that requires it to consider whether an action is necessary or appropriate in the public interest, to consider, in addition to the protection of investors, whether the action would promote efficiency, competition, and capital formation.

[189] Many commenters asserted that non-compliance with Form D filing obligations is widespread. *See, e.g.,* letters from Investor Advisory Committee (stating that ''[i]t is generally acknowledged that a significant number of issuers do not currently file Form D. . .''); AARP (stating that ''[s]imply adding a checkbox to a form that too often goes unfiled and then only after the fact is inadequate to the task at hand.''); AFL–CIO and AFR (stating that ''many issuers today flout the Form D filing requirement for such offerings, further limiting the Commission's ability to provide effective oversight''). *See also* Securities and Exchange Commission, Office of Inspector General, *Regulation D Exemption Process* (Mar. 31, 2009) (''OIG Report''), available at: *http://www.sec-oig.gov/Reports/AuditsInspections/2009/459.pdf* (stating that while the Commission staff ''strongly encourage companies to comply with Rule 503, they are aware of instances in which issuers have failed to comply with Rule 503. . .''). Based on its analysis of the filings required by FINRA Rules 5122 and 5123 during the period of December 3, 2012 to February 5, 2013, DERA estimates that as many as 9% of the offerings represented in the FINRA filings for Regulation D or other private offerings that used a registered broker did not have a corresponding Form D.

[190] *See* Ivanov/Bauguess Study.

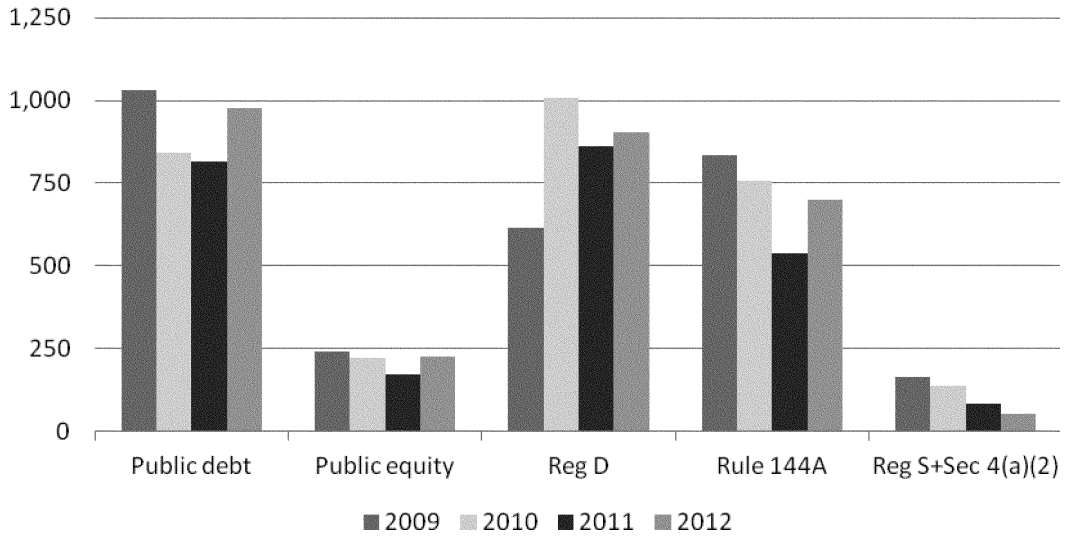
[191] *See id.*

[192] *See id.*

[193] In calculating the amount of capital raised by registered investment funds, we use the net amounts (plus reinvested dividends and reinvested capital gains), which reflect redemptions, and not gross amounts, by open-ended registered investment funds because they face frequent redemptions and do not have redemption restrictions and lock-up periods common among private funds. In addition, we use the new issuances of registered closed-end funds and the new deposits of registered unit investment trusts. *See* 2013 Investment Company Institute Factbook, available at: *http://www.icifactbook.org.*

In 2011, the estimated amount of capital (including both equity and debt) reported as being raised in Rule 506 offerings was $849 billion compared to $985 billion raised in registered offerings.[194] Of the $849 billion, operating companies reported raising $71 billion, while pooled investment funds reported raising $778 billion.[195] More generally, when including offerings pursuant to other exemptions—Rule 144A, Regulation S and Section 4(a)(2)—significantly more capital appears to be raised through exempt offerings than registered offerings (Figure 1).[196]

Figure 1: Capital Raised in U.S. Capital Markets during 2009-2012[197]



At present, issuers are required to file a Form D not later than 15 days after the first sale of securities in a Regulation D offering and an amendment to the Form D only under certain circumstances. Since issuers are not required to submit a Form D filing when an offering is completed, and submit amendments only under certain circumstances, we have no definitive information on the final amounts raised. Figure 2, below, illustrates that at the time of the Form D filing, only 39% of offerings by non-pooled investment fund issuers were completed relative to the total amount sought. Separately, 70% of pooled investment funds state their total offering amount to be ''Indefinite'' in their Form D filings. As a result, the Form D filings of these pooled investment funds likely do not accurately reflect the total amount of securities offered or sold.

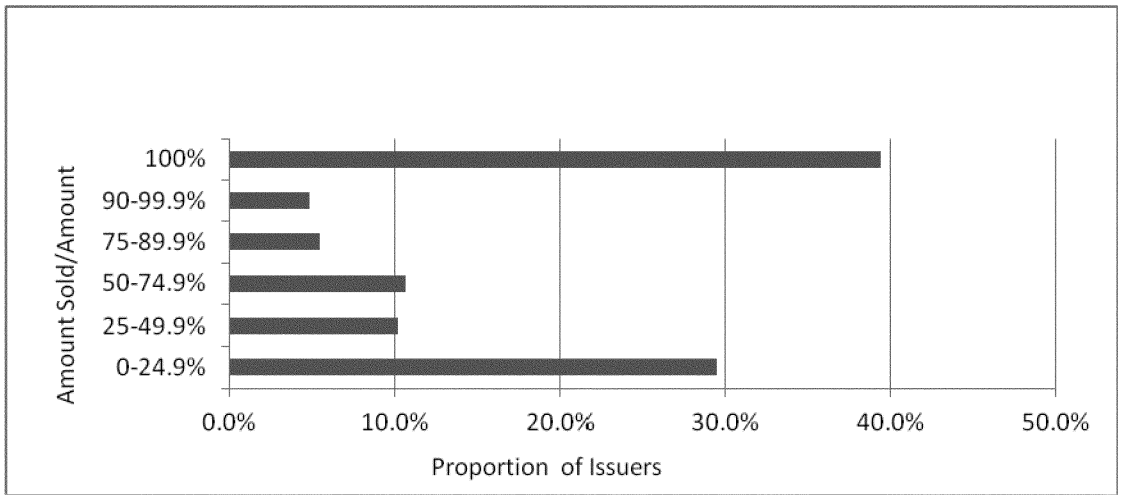
[194] *See* Ivanov/Bauguess Study.

[195] *See id.*

[196] *See id.*

[197] The 2012 non-ABS Rule 144A offerings data is based on an extrapolation of currently available data through May 2012 from Sagient Research System's Placement Tracker database. For more detail, see the Ivanov/Bauguess Study.

Figure 2: Amount Sold as Percentage of Total Offering Amount by Non-Pooled Investment Fund Issuers in Regulation D Offerings at the Time of Form D Filing: 2009-2012



2. Affected Market Participants

The amendments to Rule 506 we are adopting today will affect a number of different market participants. Issuers of securities in Rule 506 offerings include both reporting and non-reporting operating companies and pooled investment funds. Investment advisers organize and sponsor pooled investment funds that conduct Rule 506 offerings. Intermediaries that facilitate Rule 506 offerings include registered broker-dealers, finders and placement agents. Investors in Rule 506 offerings include accredited investors (both natural persons and legal entities) and non-accredited investors who meet certain ''sophistication'' requirements. Each of these market participants is discussed in further detail below.

a. Issuers

Based on the information submitted in 112,467 new and amended Form D filings between 2009 and 2012, there were 67,706 new Regulation D offerings by 49,740 unique issuers during this four-year period.[198] The size of the average Regulation D offering during this period was approximately $30 million, whereas the size of the median offering was approximately $1.5 million.[199] The difference between the average and median offering sizes indicates that the Regulation D market is comprised of many small offerings, which is consistent with the view that many smaller businesses are relying on Regulation D to raise capital, and a smaller number of much larger offerings.

Some information about issuer size is available from Item 5 in Form D, which requires issuers in Regulation D offerings to report their size in terms of revenue ranges or, in the case of certain pooled investment funds, net asset value ranges. All issuers can currently choose not to disclose this size information, however, and a significant majority of issuers that are not pooled investment funds declined to disclose their revenue ranges in the Forms D that they filed between 2009 and 2012. For those that did, most reported a revenue range of less than $1 million (Figure 3).[200] During the 2009–2011 period, approximately 10% of all public companies raised capital in Regulation D offerings; in 2012, approximately 6% of such companies did so.[201] These public companies tended to be smaller and less profitable than their industry peers, which illustrates the significance of the private capital markets to smaller companies, whether public or private.[202]

[198] *See* Ivanov/Bauguess Study.

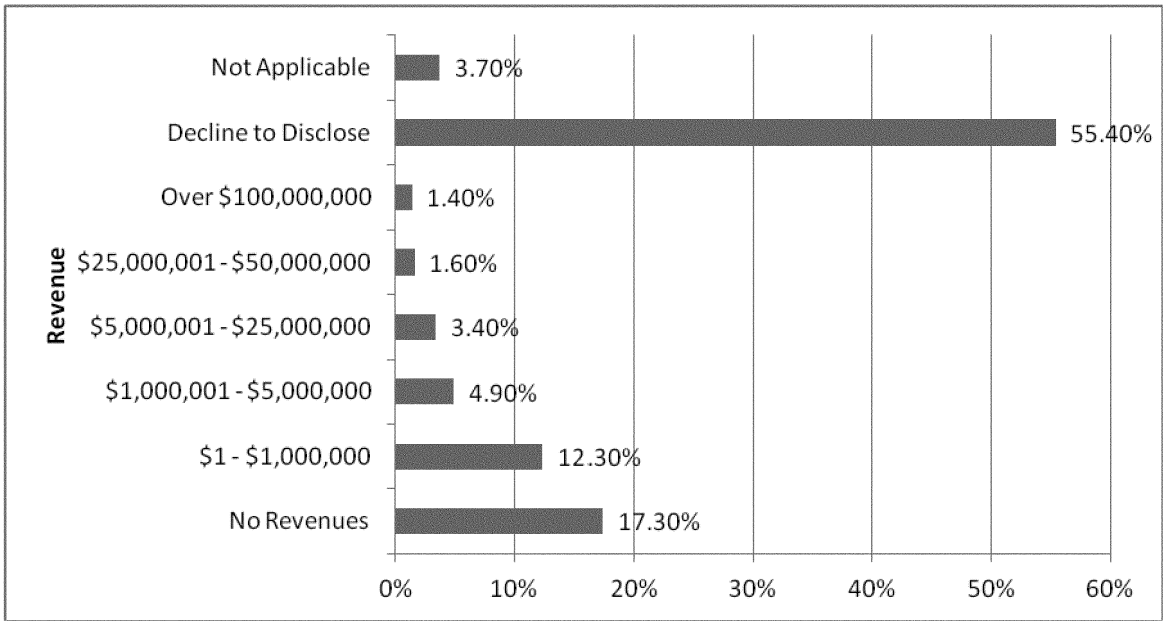
[199] *See id.* A study of unregistered equity offerings by publicly-traded companies over the period 1980–1996 found that the mean offering amount was $12.7 million, whereas the median offering amount was $4.5 million. *See* Michael Hertzel, Michael Lemmon, James Linck and Lynn Rees, *Long-Run Performance Following Private Placements of Equity,* 57 Journal of Finance 2595 (2002).

[200] *See* Ivanov/Bauguess Study.

[201] *Id.* (explaining the methodology of using listings in the Standard & Poor's Compustat database and the University of Chicago's Center for Research in Securities Prices database to determine which companies were public companies).

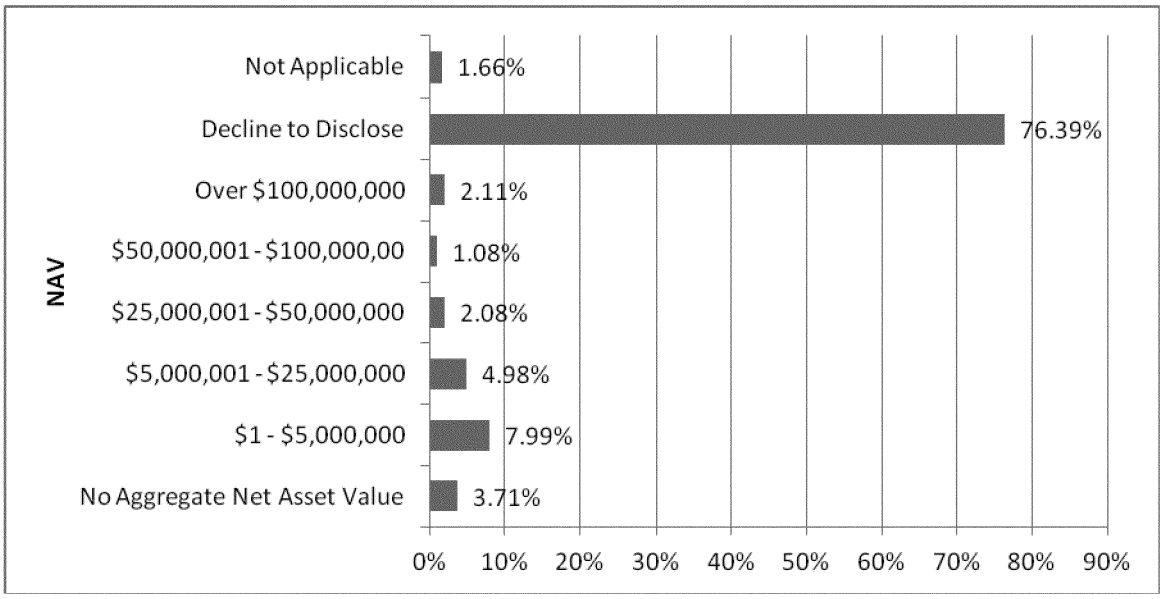
[202] *Id.*

Figure 3: Distribution of Non-Pooled Investment Fund Issuers in Regulation D Market by Revenue: 2009-2012



During this period, pooled investment funds conducted approximately 24% of the total number of Regulation D offerings and raised approximately 81% of the total amount of capital raised in Regulation D offerings.[203] More than 75% of pooled investment funds declined to disclose their net asset value range.

Figure 4: Distribution of Pooled Investment Fund Issuers in Regulation D Market by Net Asset Value: 2009-2012



Between 2009 and 2012, approximately 66% of Regulation D offerings were of equity securities, and almost two-thirds of these were by issuers other than pooled investment funds.[204] Non-U.S. issuers accounted for

[203] *Id.*

[204] *Id.*

approximately 19% of the amount of capital raised in Regulation D offerings, indicating that the U.S. market is a significant source of capital for these issuers.[205]

Unlike in Regulation D offerings, issuers conducting Rule 144A offerings are not required to disclose information about their offerings to the Commission, which limits our ability to measure the size of the Rule 144A market. Based on transaction information collected by third-party data providers,[206] we can broadly characterize the Rule 144A market as being divided between ABS and non-ABS offerings. These sources indicate that, over the four-year period from 2009 to 2012, there were 3,510 non-ABS Rule 144A offerings by 1,965 unique issuers. During this period, the average non-ABS offering size was approximately $526 million, while the median non-ABS offering size was $350 million. These offering sizes are significantly larger than the average and median amounts of Regulation D offerings, as discussed above, indicating that the Rule 144A market, as compared to the Regulation D market, is characterized by much larger issues (which we presume correlate to larger issuers, as well) and, based on the number of Rule 144A offerings, far fewer issuers. Another significant difference from Regulation D offerings is the type of security offered. During this period, over 99% of the non-ABS offerings in the Rule 144A market were debt offerings,[207] compared to 13% of Regulation D offerings.[208]

b. Investors

We have relatively little information on the types and number of investors in Rule 506 offerings. Form D currently requires issuers in Rule 506 offerings to provide information about the total number of investors who have already invested in the offering and the number of persons who do not qualify as accredited investors.[209] In 2012, approximately 153,000 investors participated in offerings by operating companies, while approximately 81,000 investors invested in offerings by pooled investment funds.[210] Because some investors participate in multiple offerings, these numbers likely overestimate the actual number of unique investors in these reported offerings. In offerings under Rule 506(b), both accredited investors and up to 35 non-accredited investors who meet certain sophistication requirements are eligible to purchase securities. In offerings under new Rule 506(c), only accredited investors will be eligible to purchase securities.

Information collected from Form D filings indicates that most Rule 506 offerings do not involve broad investor participation. More than two-thirds of these offerings have ten or fewer investors, while less than 5% of these offerings have more than 30 investors. Although Rule 506 currently allows for the participation of non-accredited investors who meet certain sophistication requirements, such non-accredited investors reportedly purchased securities in only 11% of the Rule 506 offerings conducted between 2009 and 2012.[211] Only 8% of the offerings by pooled investment funds included non-accredited investors, compared to 12% of the offerings by other issuers.[212]

[205] *Id.*

[206] These statistics are based on a review of data from Securities Data Corporation's New Issues database (Thomson Financial) and Sagient Research System's Placement Tracker database.

[207] This statistic is based on a review of data from Securities Data Corporation's New Issues database (Thomson Financial) and Sagient Research System's Placement Tracker database.

[208] *See* Ivanov/Bauguess Study.

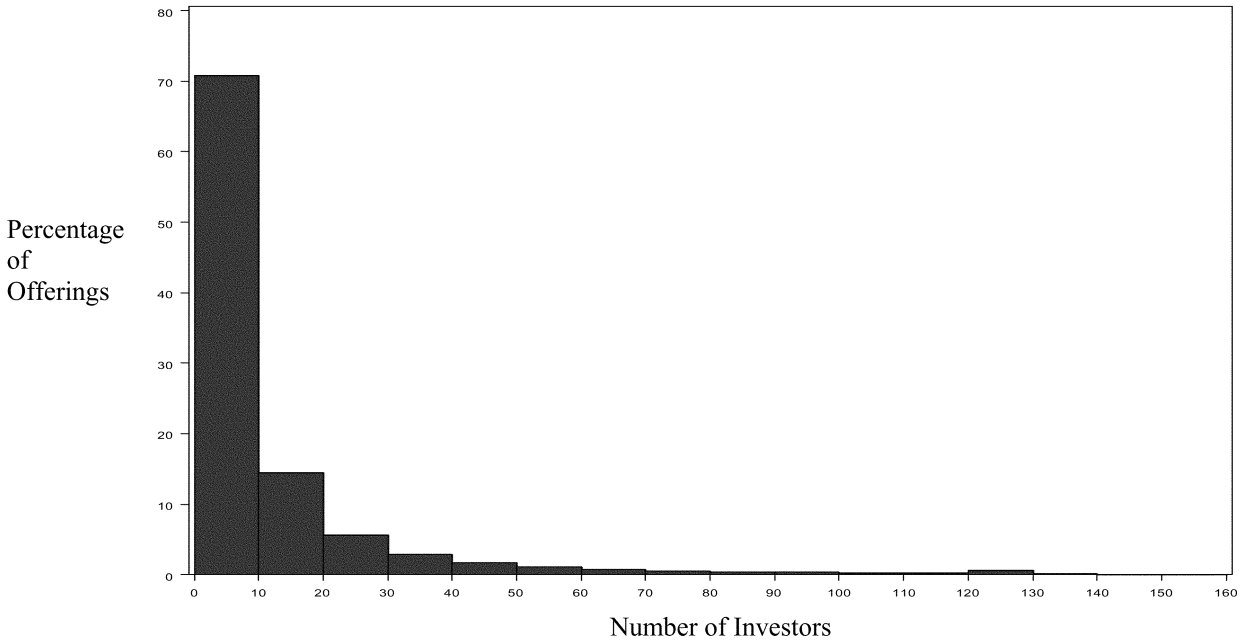
[209] *See* Item 14 of Form D. Form D does not require any other information on the types of investors, such as whether they are natural persons or legal entities.

[210] These numbers are based on initial Form D filings submitted in 2012.

[211] *See* Ivanov/Bauguess Study.

[212] *Id.*

Figure 5: Distribution of Regulation D Offerings by Number of Investors: 2009-2012



As stated above, between 2009 and 2012, the size of the median Regulation D offering, based on the information in Form D filings, was approximately $1.5 million. The presence of so many relatively small offerings suggests that a sizable number of current investors in Rule 506 offerings are natural persons or legal entities in which all equity owners are natural persons. This is because smaller offerings may not provide sufficient scale for institutional investors to earn a sizable return. Institutional investors typically have a larger investible capital base and more formal screening procedures compared to investors who are natural persons, and the associated costs of identifying potential investments and monitoring their investment portfolio lead them to make larger investments than natural persons.[213] As for whether natural persons investing in these offerings are accredited investors or non-accredited investors, almost 90% of the Regulation D offerings conducted between 2009 and 2012 did not involve any non-accredited investors.[214]

While we do not know what percentage of investors in Rule 506 offerings are natural persons, the vast majority of Regulation D offerings are conducted without the use of an intermediary,[215] suggesting that many of the investors in Regulation D offerings likely have a pre-existing relationship with the issuer or its management because these offerings would not have been conducted using general solicitation. This category of investors is likely to be much smaller than the total number of eligible investors for Rule 506(c) offerings, which is potentially very large. We estimate that at least 8.7 million U.S. households, or 7.4% of all U.S. households, qualified as accredited investors in 2010, based on the net worth standard in the definition of ''accredited investor'' (Figure 6).[216]

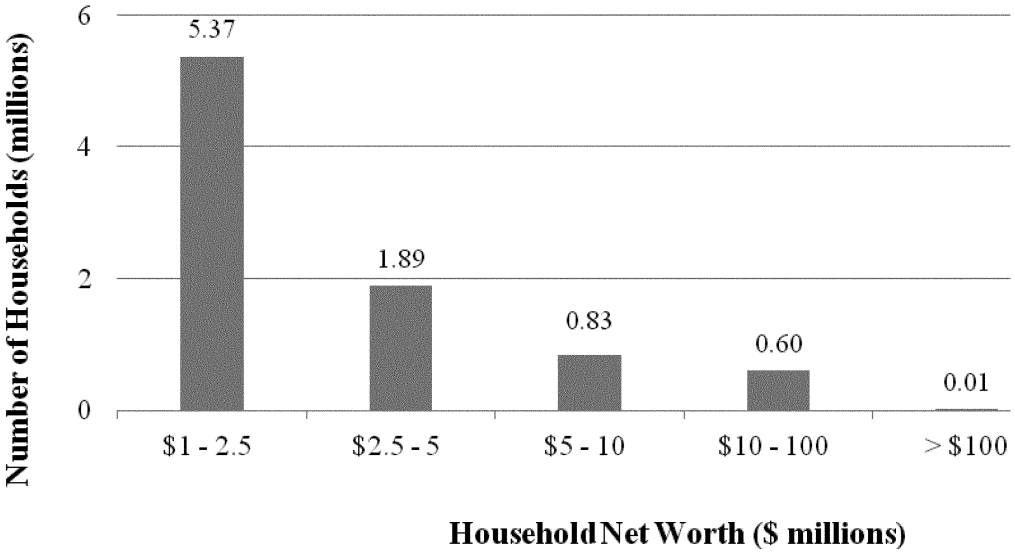
[213] *See, e.g.,* George Fenn, Nellie Liang and Stephen Prowes, The Economics of Private Equity Markets (1998); Steven Kaplan and Per Strömberg, *Leveraged Buyouts and Private Equity,* 23 Journal of Economic Perspectives 121 (2009).

[214] *See* Ivanov/Bauguess Study.

[215] An analysis of all Form D filings submitted between 2009 to 2012 shows that approximately 11% of all new offerings reported sales commissions of greater than zero because the issuers used intermediaries. *See* Ivanov/Bauguess Study. We assume that the lack of a commission indicates the absence of an intermediary.

[216] This estimate is based on net worth and household data from the Federal Reserve Board's Triennial Survey of Consumer Finances 2010. Our calculations are based on all 32,410 observations in the 2010 survey.

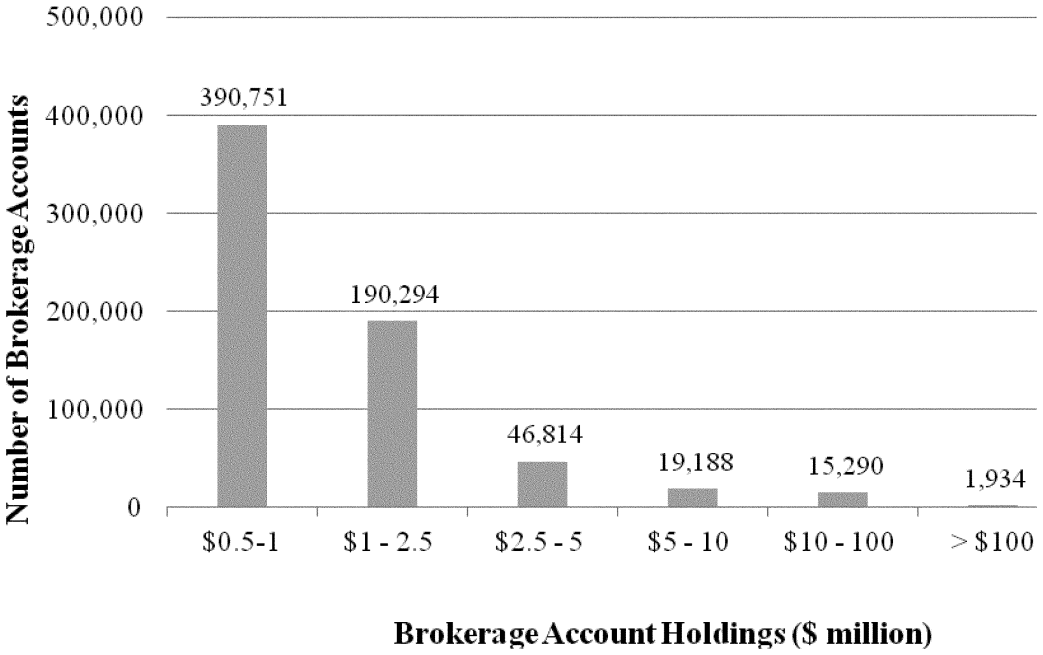
Figure 6: Number of U.S. Households that Qualify as Accredited Investors Based on 2010 Net Worth



Our analysis, however, leads us to believe that only a small percentage of these households are likely to participate in securities offerings, especially exempt offerings. First, as mentioned above, data from Form D filings in 2012 suggests that fewer than 234,000 investors (of which an unknown subset are natural persons) participated in Regulation D offerings, which is small compared to the 8.7 million households that qualify as accredited investors. Second, evidence suggests that only a small fraction of the total accredited investor population has significant levels of direct stockholdings. Based on an analysis of retail stock holding data for 33 million brokerage accounts in 2010, only 3.7 million accounts had at least $100,000 of direct investments in equity securities issued by public companies listed on domestic national securities exchanges, while only 664,000 accounts had at least $500,000 of direct investments in such equity securities (Figure 7).[217] Assuming that investments in publicly-traded equity securities are a gateway to investments in securities issued in exempt offerings, and accredited investors with investment experience in publicly-traded equity securities are more likely to participate in an exempt offering than accredited investors who do not, the set of accredited investors likely to be interested in investing in Rule 506(c) offerings could be significantly smaller than the total accredited investor population.

[217] This analysis by DERA is based on the stock holdings of retail investors from more than 100 brokerage firms covering more than 33 million accounts during the period June 2010–May 2011.

Figure 7: Direct Stock Holdings of Retail Investors, 2010



Investors in Rule 144A offerings are QIBs, which comprise a broad range of U.S. entities, including mutual funds, pension funds, banks, savings and loan associations, investment companies, insurance companies and entities whose equity owners are all QIBs.[218] As there is no obligation for issuers in Rule 144A offerings to publicly disclose the characteristics of their investors, the information available on the number and types of QIBs in the Rule 144A market is not broadly known, and is generally available only to those financial intermediaries who act as initial purchasers in the offerings.

c. Investment Advisers

As of December 2012, there were 10,870 Commission-registered investment advisers that filed Form ADV with the Commission, representing approximately $50 trillion total assets under management.[219] The average investment adviser registered with the Commission has assets under management of approximately $4.6 billion; the median size of assets under management for these registered investment advisers is $258 million.

Approximately one-fourth of registered investment advisers (2,842) currently advise (or advised) private funds that filed Form D between 2002 and 2012, while another 1,250 registered investment advisers currently advise (or advised) private funds that did not file Form D during the same period. The registered investment advisers advising private funds that submitted Form D filings during this period had average assets under management of $8.7 billion, while the ones advising private funds that did not submit Form D filings had average assets under management of $8.6 billion. Registered investment advisers that did not advise private funds (6,623) are considerably smaller, with average assets under management of $2.1 billion.

d. Broker-Dealers

As of December 2012, there were 4,450 broker-dealers registered with the Commission who file on Form X–17A–5, with average total assets of approximately $1.1 billion per broker-dealer. The aggregate total assets of these registered broker-dealers are approximately $4.9 trillion. Of these registered broker-dealers, 410 are dually registered as investment advisers. The dually registered broker-dealers are larger (average total assets of $6.4 billion) than those that are not dually registered. Among the dually registered broker-dealers, we identified 24 that currently have or have had private funds that submitted Form D filings between 2002 and 2012.

3. Current Practices

The extent of the economic impact of the amendments to Rule 506 will depend on the current practices of issuers and market participants in Rule 506 offerings. As issuers in the Regulation D market are not required to disclose in Form D how they formed a reasonable belief that the purchasers in their Rule 506 offerings are accredited investors or sophisticated investors and are not currently required to take reasonable steps to verify the accredited investor status of these purchasers, the Commission does not have any data on current verification practices used in such offerings, if any. Commenters, however, provided examples of current practices of how issuers collect information from a potential purchaser to form a reasonable belief that he or she is an accredited investor. One commenter suggested that a large number of issuers rely on lists of accredited investors created and maintained by a reliable third party, such as registered broker-dealers,[220] which would be consistent with the

[218] Non-U.S. investors generally do not participate in Rule 144A offerings; rather, they participate in Regulation S offerings. Issuers will frequently conduct side-by-side Rule 144A and Regulation S offerings.

[219] For the same time period, 2,303 exempt reporting advisers filed a Form ADV with the Commission. Certain investment advisers that are ineligible to register with the Commission may also be exempt from registration with any state.

[220] *See* letter from J. McLaughlin.

Commission's view that an issuer would not contravene Rule 502(c)'s prohibition against general solicitation if the issuer or its agent has a pre-existing substantive relationship with the offerees.[221] Other commenters asserted that many issuers rely on the services of placement agents to obtain information about accredited investor status and to complete a Rule 506 transaction.[222] One commenter stated that the most common practice was a combination of an investor suitability questionnaire and investor self-certification.[223] These commenters, however, did not provide data to allow for an estimate of the frequency of usage and the costs associated with these practices.

C. Analysis of the Amendment to Rule 506

Congress has mandated that we eliminate the prohibition against general solicitation for a subset of Rule 506 offerings.[224] Below, we analyze the benefits and costs associated with the amendments to Rule 506 in light of the baseline discussed above. Because existing Rule 506 has always been subject to the prohibition against general solicitation, there are significant data and informational limitations on our ability to quantify the economic impact of eliminating that prohibition in certain Rule 506 offerings. As discussed above, we do not believe that the Form D filings available on the Commission's Electronic Data Gathering, Analysis and Retrieval (''EDGAR'') system present a complete view of the Rule 506 market, as there are some Rule 506 offerings for which a Form D is not filed and the information presented in the Forms D that are filed is not necessarily comprehensive.[225] In addition, as discussed below, we believe that there are sufficient differences between Rule 504, as amended to permit general solicitation from 1992 to 1999, and Rule 506(c) such that it would not be useful to look to the Rule 504 market during that period to make meaningful predictions as to the type or magnitude of the effects of eliminating the prohibition against general solicitation for Rule 506(c) offerings. For example, the amount of capital that could be raised under Rule 504, as amended during this period, was capped at $1 million over a 12-month period; the securities in a Rule 504 offering could be sold to an unlimited number of non-accredited investors; and the securities sold in Rule 504 offerings were not restricted securities for purposes of resale. We provide below a qualitative analysis of the potential costs and benefits of eliminating the prohibition against general solicitation in certain Rule 506 offerings, supplementing that analysis with quantification, where possible, based on existing data.

1. Benefits to Issuers

The elimination of the prohibition against general solicitation for a subset of Rule 506 offerings will enable issuers to solicit potential investors directly, through both physical (such as mailings, newspaper advertisements and billboards) and electronic (such as the Internet, social media, email and television) means. As a result, we anticipate that issuers will be able to reach a much greater number of potential investors than is currently the case, thereby increasing their access to sources of capital. We note that many commenters, including those representing small businesses, biotechnology companies and angel investors, stated that the elimination of the prohibition against general solicitation will facilitate capital formation by allowing businesses, particularly early-stage companies, to solicit investments from a larger pool of investors.[226] This could increase overall capital formation if issuers that previously did not raise capital from individual investors because it was too costly to solicit them through intermediaries now choose to solicit investors directly using general solicitation in accordance with Rule 506(c). Alternatively, if issuers use new Rule 506(c) in lieu of other methods of raising capital, such as registered offerings or unregistered non-Rule 506(c) offerings, then Rule 506(c) would replace one source of capital for another, thereby potentially improving the efficiency of capital flow through lower issuance costs, but not necessarily increasing the gross amount raised.

We believe that it is reasonable to conclude that allowing issuers to have wider access to accredited investors by eliminating the prohibition against general solicitation for a category of Rule 506 offerings will significantly improve their access to capital and potentially enhance capital formation and lower the issuance cost. Although the lack of available data on the economic impact of eliminating the prohibition against general solicitation in Rule 506 offerings precludes us from quantifying the magnitude of this effect, the Commission has some evidence of the effect of the availability of general solicitation on issuers' ability to raise capital based on information about the number of Rule 504 offerings from 1992 to 2001, which covers the period during which the prohibition against general solicitation was lifted for Rule 504,[227] and subsequently reinstated in 1999.[228] In particular, and as shown in the chart below, the number of Rule 504 offerings increased at an average annual rate of 10.6% from 1992 through 1999.[229] In 2000, following the reinstatement of the ban, the number of Rule 504 offerings declined by almost 44%. This decline is coincident with the general market decline in 2000, including the collapse of the Internet bubble, which may have been the cause or at least a significant contributing factor to the rate of decline. During 2000, however, there was not a concurrent decline in either the number of Rule 505 offerings or the number of Rule 506 offerings. To the contrary, the number of Rule 506 offerings increased by about 54% in 2000, while the number of Rule 505 offerings remained largely unchanged (Figure 8). Declines in the numbers of Rule 505 and Rule 506 offerings followed in 2001, when presumably both types of offerings were

[221] *See* Release No. 33–7856.

[222] *See* letters from SIFMA and FSR (Oct. 5, 2012); IAA.

[223] *See* letters from NSBA; MFA (May 4, 2012) (noting that, in the hedge fund industry, a potential hedge fund investor must complete ''a subscription document provided by the fund's manager that provides a detailed description of, among other things, the qualification standards that a purchaser must meet under the federal securities laws'').

[224] The legislative history of a bill that was introduced (but not adopted) at or around the time of the JOBS Act may be instructive with respect to how Congress viewed the effect of eliminating the prohibition against general solicitation in private offerings. In its report on a bill that would have amended Section 4(a)(2) of the Securities Act to permit the use of general solicitation, the House Committee on Financial Services stated that ''regulations such as the prohibition of general solicitation and advertising in Regulation D Rule 506 offerings inhibit capital formation.'' Access to Capital for Job Creators Act, H.R. Rep. 112–263, at 2 (2011). Accordingly, ''[t]he legislation would allow companies greater access to accredited investors and to new sources of capital to grow and create jobs, without putting less sophisticated investors at risk.'' *Id.*

[225] Because filing a Form D is not a condition for relying on Regulation D, commenters have noted that many issuers do not file a Form D when raising capital under Rule 506. Issuers are currently required to file an initial Form D within 15 days of the first sale of securities, but are required to report additional sales through amended filings only under certain conditions, which means that in many cases, the total amount of capital raised in a Regulation D offering is not reported on Form D. Finally, issuers do not report all required information, either due to error or because they do not wish to make the information public. For example, issuers have the option in Form D to decline to disclose their revenues or net asset values.

[226] *See, e.g.,* letters from BIO; NSBA.

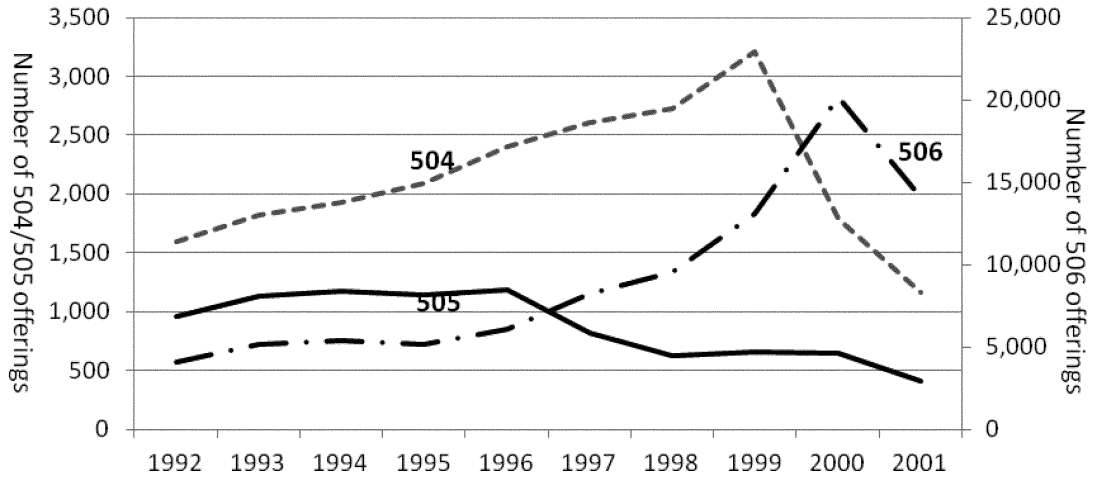
[227] *See Small Business Initiatives,* Release No. 33–6949 (July 30, 1992) [57 FR 36442 (Aug. 13, 1992)].

[228] *See* Release No. 33–7644.

[229] This is based on an analysis of Form REGDEX filings on EDGAR.

negatively affected by the general market decline, although Rule 504 offerings experienced a sharper decline (−35%) compared to Rule 506 offerings (−30%). While it is not possible to disentangle the broader market effects in 2000 from the reinstatement of the prohibition against general solicitation on the number of Rule 504 offerings, the steady increase in the number of Rule 504 offerings during the seven-year period following the elimination, in 1992, of the prohibition against general solicitation and the subsequent sharp decline in the number of Rule 504 offerings is consistent with the view that issuers' ability to generally solicit may enhance their ability to raise capital.

Figure 8: Number of New Regulation D Offerings: 1992-2001



The development of the venture capital (VC) industry in the United States may also be a relevant example to illustrate the potential for enhanced capital formation that may result from allowing issuers to have access to a wider range of investors. Under the Employment Retirement Income Security Act of 1974, pension fund managers are subject to a ''prudent man'' standard of care in making investments.[230] Prior to 1979, there was uncertainty under the U.S. Department of Labor's then-existing interpretations of this standard as to whether pension funds could invest in venture capital and start-up companies. In 1979, the Department clarified its interpretation of this standard by indicating that portfolio diversification is a factor in determining whether an investment is prudent, which indicated that pension funds would not be precluded from making investments in VC funds.[231] Following this regulatory change, the VC industry experienced substantial growth: VC commitments increased from $218 million in 1978 (of which pension funds supplied approximately 15%) to $3 billion in 1988 (of which pension funds supplied approximately 46%).[232]

We also anticipate that allowing issuers to solicit potential investors directly will lower the direct costs of Rule 506 offerings. Although none of the commenters provided data on direct cost savings, and although Form D filings do not present a complete view of the market, we do have estimates of the direct offering costs paid by issuers that use an intermediary to locate investors in Rule 506 offerings. An analysis of all Form D filings submitted between 2009 to 2012 shows that approximately 11% of all new Regulation D offerings reported sales commissions of greater than zero because the issuers used intermediaries.[233] The average commission paid to these intermediaries was 5.9% of the offering size, with the median commission being approximately 5%. Accordingly, for a $5 million offering, which was the median size of a Regulation D offering with a commission during this period, an issuer could potentially save up to $250,000 if it solicits investors directly rather than through an intermediary, minus the cost of its own solicitation efforts and the cost associated with verifying accredited investor status.[234] This potential benefit would likely be larger on a percentage basis for smaller offerings. During this four-year period, of the issuers that paid a commission in connection with a Regulation D offering, issuers raising up to $1 million in capital paid on average a 6.5% commission, whereas issuers raising over $50 million in capital paid on average a 1.9% commission.[235]

Even for issuers that do not currently use an intermediary, allowing issuers to generally solicit would likely lower the search costs associated with finding accredited investors who would be interested in a particular offering, thus enhancing economic efficiency.[236] If lower search costs expand the pool of interested investors for offerings, there could be greater competition among

[230] 29 U.S.C. 1104(a).

[231] *See* 29 CFR 2550.404a–1(b)(1)(i).

[232] *See* Paul A. Gompers and Josh Lerner, The Venture Capital Cycle (2006); Paul Gompers, *The Rise and Fall of Venture Capital,* 23 Business and Economic History 1 (1994).

[233] *See* Ivanov/Bauguess Study.

[234] We recognize that intermediaries can provide benefits to issuers in addition to locating investors. For example, an intermediary may be able to help an issuer obtain better pricing and terms or provide access to investors that can provide strategic or other advice to the issuer. An intermediary could also provide accreditation services. Unfortunately, we do not have data to quantify these benefits.

[235] *See* Ivanov/Bauguess Study.

[236] See, for example, Erik Sirri and Peter Tufano, *Costly Search and Mutual Fund Flows,* 53 Journal of Finance 1589 (1998), for a similar argument with respect to investors in mutual funds.

investors, thereby lowering the costs of capital for issuers.[237]

The elimination of the prohibition against general solicitation would also reduce the uncertainty for issuers as to whether a Rule 506 offering can be completed in certain situations, and would eliminate the costs of complying with the prohibition.[238] Under existing Rule 506, an inadvertent release of information about an offering to entities or persons with whom the issuer does not have a pre-existing substantive relationship has been viewed by some as raising questions about the issuer's ability to rely on the exemption for the entire offering.[239] In addition, some private funds have been reluctant to respond to press inquiries or to correct inaccurate reports due to concerns about these discussions being misconstrued as a general solicitation.[240] Under Rule 506(c), any such uncertainty as to the availability of the exemption due to the public disclosure of information will be reduced. Nevertheless, there is no data available to quantify or estimate these effects.

2. Benefits to Investors

The elimination of the prohibition against general solicitation in Rule 506(c) offerings will likely increase the amount and types of information about issuers and offerings that are communicated to investors, which could also lead to more efficient pricing for the offered securities. In addition, accredited investors who previously have found it difficult to find investment opportunities in Rule 506 offerings may be able to find and potentially invest in a larger and more diverse pool of potential investment opportunities, which would result in a more efficient allocation of investments by accredited investors.[241] Thus, Rule 506(c) could increase capital formation and at the same time improve its allocative efficiency.[242] One commenter argued that we do not provide data to support the statements that accredited investors need new opportunities or cannot find new opportunities under the current rules prohibiting the use of general solicitation in Rule 506 offerings.[243] While we do not have data to test the validity of these statements since general solicitation has heretofore been prohibited in Rule 506 offerings, economic theory suggests that expanding investors' opportunities for investment generally results in more efficient allocation of capital. For example, one seminal study suggests that if some investors have incomplete information and are not aware of all firms in the economy, risk sharing is incomplete and inefficient.[244] Information that makes investors aware of the existence of these firms and enlarges the investor base leads to improved risk sharing and lower cost of capital.

With respect to private funds in particular, in the Proposing Release, we noted that eliminating the prohibition against general solicitation would allow accredited investors to gather information about private funds at relatively lower costs and to allocate their capital more efficiently.[245] Increased information about private fund strategies, management fees and performance information would likely lead to greater competition among private funds for investor capital.

Some commenters noted that greater transparency about private funds' activities would benefit investors in these funds, and communications about these activities would be subject to the antifraud provisions of the federal securities laws and FINRA regulations on the preparation of marketing materials.[246] Other commenters believed that private funds engaging in general solicitation should be subject to form, content and/or other restrictions, such as performance and advertising standards that are analogous to the standards that are applicable to mutual funds in order to engage in general solicitation.[247] One of the commenters suggested that the Commission develop a rule tailored to the ways private funds calculate and present performance, rather than extending mutual fund performance rules to private funds.[248] With respect to private funds sold through broker-dealers subject to FINRA's rules of conduct, some commenters believed that we should direct FINRA to require the filing and review of private fund advertisements.[249]

While the lack of data does not allow us to quantify the costs and benefits of eliminating the prohibition against general solicitation under Rule 506(c) for private funds, we believe that the potential for an increase in fraudulent or deceptive issuer behavior due to the elimination of the prohibition may be limited to some extent by the competitive nature of the private funds industry as well as by the fact that there are often repeat interactions between private funds and their investors.[250]

3. Costs

Eliminating the prohibition against general solicitation could result in heightened fraudulent activity in Rule 506(c) offerings because it will be easier for promoters of fraudulent schemes to reach potential investors through general solicitation. An increase in fraud would not only harm those investors who are defrauded, it would undermine investor participation in Rule 506(c) offerings and could negatively affect capital-raising by legitimate issuers—for example, by reducing investor participation in Rule 506(c) offerings—thereby inhibiting capital formation and reducing efficiency. One commenter was concerned that investors may confuse private funds with registered investment companies.[251] In such cases, fraud that occurs with private funds may cause

[237] For example, a study on offerings involving venture capitalists finds that increased competition among them results in higher valuations for issuers. *See* Paul Gompers and Josh Lerner, *Money Chasing Deals? The Impact of Fund Inflows on Private Equity Valuations,* 55 Journal of Financial Economics 281 (2000).

[238] *See* letter from MFA (May 4, 2012).

[239] *See, e.g.,* letter from S. Lorne and J. McLaughlin (Aug. 5, 2008) on Release No. 33–8828 (stating that ''[o]n occasion, the prohibition forces issuers to delay or even cancel offerings because of communications—sometimes inadvertent—that could be viewed in hindsight as a solicitation. The need to police communications by transaction participants, and to analyze and remedy inadvertent communications, also adds significantly to the cost of effecting private placements.'').

[240] *See, e.g.,* letters from D.E. Shaw & Co. (Apr. 3, 2006) on *Exposure Draft of Final Report of Advisory Committee on Smaller Public Companies,* Release No. 33–8666 (Feb. 28, 2006); MFA (May 4, 2012).

[241] This benefit may not be applicable with respect to every issuer (*e.g.,* certain private funds that offer their shares continuously at net asset value).

[242] Allocative efficiency is a condition that is reached when resources are allocated in a way that allows the maximum possible net benefit from their use. In this context, it means the right number of dollars from the right types of investors going to the most suitable investments on efficient terms.

[243] *See* letter from Consumer Federation.

[244] *See* Robert Merton, *A Simple Model of Capital Market Equilibrium With Incomplete Information,* 42 Journal of Finance 483 (1987).

[245] *See, e.g.,* letter from MFA (May 4, 2012); and Managed Funds Association, Petition for Rulemaking on Rule 502 of Regulation D under the Securities Act of 1933, File No. 4–643 (Jan. 9, 2012) (''MFA Petition'').

[246] *See* letters from IAA; BlackRock; MFA (Sept. 28, 2012).

[247] *See, e.g.,* letters from AFL–CIO and AFR; Sen. Levin; Consumer Federation; Fund Democracy; Investor Advisory Committee; ICI; IDC; Rep. Waters; NASAA; P. Turney; and Sens. Reed, Levin, Durbin, Harkin, Lautenberg, Franken and Akaka.

[248] *See* letter from ICI.

[249] Letters from AFL–CIO and AFR; ICI.

[250] *See, e.g.,* William Fung and David Hsieh, *Hedge Fund Benchmarks: Information Content and Biases,* 58 Financial Analysts Journal 22 (2002); Rajarishi Nahata, *Venture Capital Reputation and Investment Performance,* 90 Journal of Financial Economics 127 (2008); Douglas Cumming and Uwe Walz, *Private Equity Returns and Disclosure Around the World,* 41 Journal of International Business Studies 727 (2010).

[251] *See* letters from ICI; ICI re: MFA Petition (Feb. 7, 2012).

investors to associate the wrongdoing with registered investment companies, and therefore refrain from investing in registered investment companies. In addition, some issuers with publicly-traded securities may use general solicitation for a purported Rule 506(c) offering to generate investor interest in the secondary trading markets, especially in the over-the-counter markets, which could be used by insiders to resell securities at inflated prices. This would impose costs to investors in these secondary markets, as well as investors in Rule 506(c) offerings, and could erode investor participation in Rule 506(c) offerings, thus potentially raising the cost of capital for issuers in this market. As discussed above, we cannot quantify these potential costs because the existence of the prohibition against general solicitation in Rule 506 offerings until now means that data on the economic impact of eliminating the prohibition is not available.

Several commenters echoed concerns regarding the potential of fraud related to private funds in the Rule 506(c) market.[252] Empirical evidence on the extent of fraud involving private funds is not readily available. While a few economic studies suggest that certain hedge funds engage in various types of misreporting, such as misrepresenting past performance,[253] delaying disclosure of returns [254] and inflating returns at the end of the fiscal year in order to earn higher fees,[255] these studies do not provide information about the extent or magnitude of any such misreporting activities. In a 2003 report, the Commission staff noted that there was no evidence that hedge funds were disproportionately involved in fraudulent activity and that the charges brought by the Commission in 38 enforcement actions against hedge fund advisers and hedge funds between 1999 and 2003 were similar to the charges against other types of investment advisers.[256] Evidence on the extent of fraud involving other types of pooled investment funds also is sparse. A more recent study has identified 245 lawsuits (both federal and state) involving 200 venture capitalists as defendants between 1975 and 2007, and has shown that VC funds that are older and have a larger presence in terms of size and network are less likely to be sued.[257]

A number of commenters [258] noted the Commission's experience with the elimination of the prohibition against general solicitation for Rule 504 offerings in 1992,[259] and its subsequent reinstatement in 1999 as a result of heightened fraudulent activity.[260] We do not believe that our experience with offerings conducted pursuant to Rule 504, as amended in 1992, is particularly instructive with respect to the potential incidence of fraud resulting from our implementation of Section 201(a) of the JOBS Act, for a number of reasons. In 1992, when we amended Rule 504 to eliminate the prohibition against general solicitation, we also provided that the securities issued in these Rule 504 offerings would not be ''restricted securities'' for purposes of resale pursuant to Rule 144 under the Securities Act.[261] As a result, a non-reporting company could sell up to $1 million of immediately freely-tradable securities in a 12-month period and be subject only to the antifraud and civil liability provisions of the federal securities laws.

By 1998, we concluded that securities issued in these Rule 504 offerings facilitated a number of fraudulent secondary transactions in the over-the-counter markets, and that these securities were issued by ''microcap'' companies, characterized by thin capitalization, low share prices and little or no analyst coverage.[262] At that time, we stated that, while ''we believe that the scope of abuse is small in relation to the actual usage of the exemption, we also believe that a regulatory response may be necessary.'' [263] As the freely-tradable nature of the securities facilitated the fraudulent secondary transactions, we proposed to ''implement the same resale restrictions on securities issued in a Rule 504 transaction as apply to transactions under the other Regulation D exemptions,'' in addition to reinstating the prohibition against general solicitation. Although we recognized that resale restrictions would have ''some impact upon small businesses trying to raise 'seed capital' in bona fide transactions,'' we believed that such restrictions were necessary so that ''unscrupulous stock promoters will be less likely to use Rule 504 as the source of the freely tradable securities they need to facilitate their fraudulent activities in the secondary markets.'' [264]

In contrast, issuers using Rule 506(c) can sell only to accredited investors, and the securities issued in these offerings are deemed to be ''restricted securities'' for purposes of resale under Rule 144. As a result, schemes involving price manipulation to defraud unknowing investors in the immediate resale of securities purchased directly from issuers (colloquially referred to as ''pump and dump'' schemes) [265] are not the types of fraud we believe are likely to occur in Rule 506(c) offerings, given the holding period requirement in Rule 144(d) and other structural impediments, such as restricted transfer legends on stock certificates.

The risks to investors of fraudulent offerings conducted under Rule 506(c) may be mitigated to some extent by the requirement that issuers sell only to accredited investors (and take reasonable steps to verify such status), who, by virtue of meeting the requirements of the definition, may be better able to assess their ability to take financial risks and bear the risk of loss than investors who are not accredited investors. Issuers will still be subject to the antifraud provisions under the federal securities laws, and the public nature of these solicitations may also facilitate detection of fraudulent activity in that the fraudulent nature of some offerings may be inferred from particular statements contained in solicitation materials, for example, representations of guaranteed high rates of return.

Several commenters asserted that satisfying the definition of accredited investor does not equate to financial sophistication and that it is questionable whether accredited investors will be better able to identify the financial risks

[252] *See* letters from Consumer Federation; Fund Democracy; IDC.

[253] *See* Andrew Patton, Tarun Ramadorai, and Michael Streatfield, *Change You Can Believe In? Hedge Fund Data Revisions* (Duke University, Working Paper, 2013). *But see* letter from MFA (June 20, 2013) (questioning the reliability of the underlying data used in the study).

[254] *See* George Aragon and Vikram Nanda, *Strategic Delays and Clustering in Hedge Fund Reported Returns* (Arizona State University, Working Paper, 2013).

[255] *See* Vikas Agarwal, Naveen Daniel, and Naranyan Naik, *Do Hedge Funds Manage Their Reported Returns?,* 24 Review of Financial Studies 3282 (2011).

[256] *See* Staff Report on Hedge Funds.

[257] *See* Vladimir Atanasov, Vladimir Ivanov, and Kate Litvak, *Does Reputation Limit Opportunistic Behavior in the VC Industry? Evidence From Litigation Against VCs,* 67 Journal of Finance 2215 (2012).

[258] *See* letters from Consumer Federation; Fund Democracy; Sen. Levin.

[259] *See* Release No. 33–6949.

[260] *See* Release No. 33–7644.

[261] 17 CFR 230.144.

[262] *Revision of Rule 504 of Regulation D, the ''Seed Capital'' Exemption,* Release No. 33–7541 (May 21, 1998) [63 FR 29168 (May 28, 1998)].

[263] *Id.* at 29169.

[264] *Id.*

[265] *See, e.g.,* Testimony of Arthur Levitt, Chairman, U.S. Securities and Exchange Commission, before the Permanent Subcommittee on Investigations, Senate Committee on Governmental Affairs, Sept. 22, 1997; *SEC* v. *Huttoe,* Litigation Release No. 15237 (Jan. 31, 1997), 63 SEC Docket 2383 (Mar. 4, 1997); *SEC* v. *Spencer,* Litigation Release No. 14856 (Mar. 29, 1996), 61 SEC Docket 1960 (Apr. 30, 1996), and Litigation Release No. 15042 (Sept. 12, 1996), 62 SEC Docket 2409 (Oct. 8, 1996).

of the offerings and detect fraudulent offerings as compared to non-accredited investors.[266] They also noted that the income test and the net worth test have been significantly eroded by inflation. These commenters also stated that not all general solicitation activities are widely known or accessible, and that fraudulent offerings sold through telemarketing calls and email solicitations, for example, will be difficult if not impossible to detect until after significant damage has occurred.

4. Indirect Effects on Other Markets

Although Rule 506(c) will directly affect the private offering market, it could also have an indirect effect on other markets. The lower search costs associated with finding Rule 506(c) offerings may cause some investors that currently invest in public equity and debt markets or other non-registered offering markets to reallocate capital to offerings made under Rule 506(c). If a significant number of investors make a greater proportion of their investments in Rule 506(c) offerings, such investor behavior may reduce the supply of capital and prices in the public equity and debt markets and in other non-registered offering markets. For example, issuers currently using the exemptions in Regulation A under the Securities Act [267] and in Rules 504(b)(1)(i) through (iii) of Regulation D [268] to solicit investors could prefer to rely on the exemption under Rule 506(c) because they would be able to raise unlimited amounts of capital under Rule 506(c) and state blue sky securities registration requirements do not apply to Rule 506(c) offerings.[269] Although it is difficult to estimate how many of these issuers will choose to rely on Rule 506(c) in lieu of other available exemptions from registration, we believe that it is likely that Rule 506(c) will have a larger impact on issuers using Rule 504 rather than Regulation A because very few issuers have been using the Regulation A exemption in recent years.[270] In addition, to the extent that accredited investors have invested in registered investment companies instead of private funds because of information asymmetry between private funds and registered investment companies, it is possible that registered investment companies' assets may decrease if these investors now transfer their assets to private funds. Because we cannot predict how issuers will use the various exemptions from registration after the elimination of the prohibition against general solicitation in Rule 506(c) offerings, we cannot quantify these potential effects.

5. Retention of Rule 506(b)

We believe that retaining existing Rule 506(b) will have benefits for both issuers and investors. It will allow issuers that do not wish to generally solicit in their private offerings to avoid the added expense of complying with the rules applicable to Rule 506(c) offerings. It will also allow issuers to continue selling privately to up to 35 non-accredited investors who meet existing Rule 506's sophistication requirements. The continued availability of Rule 506(b) may also be beneficial to investors with whom the issuer has a pre-existing substantive relationship and who do not wish to bear additional verification costs that may be associated with participation in Rule 506(c) offerings. All but one commenter supported the Commission's decision to retain Rule 506(b).[271]

D. Verifying Accredited Investor Status in Rule 506(c) Offerings

As there is no information available to us on the costs currently incurred by issuers to form a reasonable belief that a purchaser in a Rule 506 offering is an accredited investor, we are unable to quantify the estimated costs and benefits of the verification requirement in Rule 506(c). Comments from the public on this issue also did not provide any estimates.

The requirement in Rule 506(c) for issuers to take reasonable steps to verify that purchasers are accredited investors will likely make it more difficult for issuers to sell securities to non-accredited investors. This, in turn, may reduce the likelihood that fraudulent offerings would be completed because those who are eligible to purchase are more likely to be able to protect their interests than investors who are not accredited investors. Issuers would also benefit from measures that improve the integrity and reputation of the Rule 506(c) market because the measures would facilitate investor participation, which could result in issuers having greater access to capital.

The verification requirement in Rule 506(c) would impose costs as well. Because the requirement is to take ''reasonable'' steps to verify, and not every conceivable step to verify, it is possible that some investors in Rule 506(c) will not be accredited investors, even if the issuer takes reasonable steps to verify their status as accredited investors. If so, then these investors will participate in offerings for which they are not qualified and that may not be appropriate for them, thereby resulting in a potentially inefficient allocation of capital for these investors. These investors could also face an additional cost in the form of heightened risk of significant losses on their investments, which they may not be able to manage or diversify in a way that accredited investors could.

In addition, some potential investors likely would have to provide more information to issuers than they currently provide, while issuers may have to apply a stricter and more costly process to determine accredited investor status than what they currently use. While commenters provided us with examples of the methods currently used by issuers in the Rule 506 market to collect information about purchasers, they did not provide any data on the costs of these methods. While it is reasonable to expect that the costs associated with the verification requirement could be offset somewhat by its benefits, it is also reasonable to expect that some accredited investors who would participate in existing Rule 506(b) offerings would decline to participate in Rule 506(c) offerings in light of the verification requirement.

To the extent that issuers require investors to provide personally identifiable information (*e.g.,* Social Security numbers, tax information, bank or brokerage account information) in order to verify their accredited investor status, these investors may be reluctant to do so in the context of making an investment in an issuer, particularly an issuer with which they may have no prior relationship.[272] In addition to concerns about maintaining personal privacy, investors may be concerned that their personally identifiable information could be stolen or accessed by third parties or used by

[266] *See, e.g.,* letters from Consumer Federation; Fund Democracy.

[267] 17 CFR 230.251 through 17 CFR 230.263.

[268] 17 CFR 230.504(b)(1)(i)–(iii).

[269] 17 CFR 230.251 through 17 CFR 230.263.

[270] The Ivanov/Bauguess Study reported that 1,852 issuers relied on the Rule 504 exemption to raise capital between 2009 to 2012, and 20 issuers relied on Regulation A. The number of issuers using Regulation A to raise capital may increase once the Commission adopts rules implementing Title IV of the JOBS Act, which directs the Commission to adopt an exemption based on Regulation A to permit offerings of up to $50 million.

[271] *See, e.g.,* letters from ABA Fed. Reg. Comm.; ACA (Sept. 27, 2012); CFIRA; IPA; Montgomery & Hansen; NSBA; NYCBA; S&C; SIFMA and FSR (Oct. 5, 2012). Only one commenter opposed retaining it. Letter from J. McLaughlin (stating that ''[t]here is no basis in the statute for the Commission to continue to apply the prohibition to a set of offerings exempt under Rule 506, especially since the effect of maintaining a parallel rule may have the effect of discouraging some issuers from using general solicitation . . . .'').

[272] *See* letter from SecondMarket Holdings, Inc. (May 25, 2012).

unscrupulous issuers in various ways (*e.g.,* identity theft), which could impose costs to investors that go well beyond the costs typically associated with investing. As a consequence, some potential investors may elect not to participate in Rule 506(c) offerings, thus impeding capital formation to some extent.

Our decision not to specify the verification methods that an issuer must use in taking reasonable steps to verify accredited investor status would provide issuers with the flexibility to use methods that are appropriate in light of the facts and circumstances of each offering and each purchaser. Such flexibility could mitigate the cost to issuers of complying with Rule 506(c) because it would allow them to select the most cost-effective verification method for each offering. We anticipate, however, that issuers or their verification service providers will document the particular verification methods used in the event of any question being raised about the availability of the exemption. Although we do not specify the nature or extent of any such documentation, we acknowledge that it will create some cost.

On the other hand, the greater flexibility of the principles-based ''reasonableness'' verification method could result in less rigorous verification, thus allowing some unscrupulous issuers to more easily sell securities to purchasers who are not accredited investors and perpetrate fraudulent schemes, or it could create or promote legal uncertainty about the availability of Rule 506(c), which may cause some issuers to interpret ''reasonable steps to verify'' in a manner that is more burdensome than if specific verification methods were prescribed, thus incurring higher cost. We believe that the non-exclusive list of specific methods of verification we are including in Rule 506(c), as adopted, should help to mitigate the impact of these costs.

Some commenters suggested that using a flexible verification standard is optimal for issuers because it closely resembles current market practices which they believe have worked well in this market.[273] Such flexibility will allow issuers to adopt different approaches based on the types of accredited investors, types of offerings and changing market practices. In contrast, other commenters questioned the benefits of the flexibility provided by the principles-based verification method and criticized the Commission for not quantifying the costs and benefits of currently used verification methods.[274] They argued that the application of the reasonableness standard in the principles-based method will lead to lax verification practices by issuers, which would lessen investor protection by allowing sales of securities to non-accredited investors.

Our decision to provide a non-exclusive list of specified methods that issuers can use to verify a purchaser's accredited investor status will provide legal certainty in those circumstances in which there is a question as to whether or not the steps taken are reasonable in light of the facts and circumstances. Using a specified method would reduce issuers' verification costs to the extent that they would otherwise incur costs to analyze whether or not the steps they had taken or proposed to take satisfied the reasonableness standard in Rule 506(c). It could also reduce investors' costs, since the methods for verifying income and net worth rely mostly on documents prepared by third parties at no cost to the investors. On the other hand, some investors may be reluctant to provide the personal financial information required by the income and net worth methods; and with respect to the third-party method, it may be relatively costly to pay for the verification services of a lawyer or accountant as they may be concerned about professional liability. The grandfather method—which permits self-certification by existing investors who purchased securities as accredited investors in an issuer's Rule 506(b) offering before the effective date of Rule 506(c)—could result in investors that do not meet the definition of ''accredited investor'' participating in Rule 506(c) offerings because issuers conducting Rule 506(b) offerings are not required to take reasonable steps to verify the accredited investor status of their purchasers.

In addition, our non-exclusive list of specified verification methods could be mistakenly viewed by market participants as the required verification methods, in which compliance with at least one of the enumerated methods could be viewed, in the practical application of the verification requirement, as necessary in all circumstances to demonstrate that the verification requirement has been satisfied, thereby eliminating the flexibility that Rule 506(c) is intended to provide.[275] If issuers choose not to use verification methods different from those on the non-exclusive list, then some potential investors may limit their participation in the Rule 506(c) market, which may impede capital formation to some extent. Finally, even if a specified method has been used, thereby satisfying the verification requirement, there may be circumstances in which issuers may unreasonably overlook or disregard other information indicating that a purchaser is not, in fact, an accredited investor. This could lead to sales being made to persons who are not accredited investors. Because, as stated above, the Commission does not have data on current verification practices, we cannot quantify the effect of the new verification requirement in Rule 506(c).

E. Analysis of the Amendment to Rule 144A

We expect the potential benefits of the amendments to Rule 144A to be lower (*i.e.,* less available) for issuers in Rule 144A offerings as compared to issuers in Rule 506(c) offerings because QIBs, which are the only permitted investors in Rule 144A offerings, are generally fewer in number, known by market participants, and better networked than accredited investors. Thus, as we noted in the Proposing Release, we believe that eliminating the prohibition against general solicitation for Rule 144A offerings is unlikely to dramatically increase issuers' access to QIBs in such offerings or to lower the cost of capital in Rule 144A offerings.

We expect that there would be fewer potential occurrences of general solicitation-induced fraud in Rule 144A offerings, as compared to Rule 506(c) transactions, because Rule 144A offerings involve an intermediary that, as the initial purchaser of the securities, typically performs a due diligence investigation and assists the issuer in preparing the offering materials, thereby adding a layer of protection against fraud. Also, Rule 144A investors are generally large institutions, which are thought to be better able to identify fraudulent activities than smaller institutions and retail investors in general.

We also anticipate that eliminating the prohibition against general solicitation would significantly affect private trading systems by permitting information vendors to provide more information about Rule 144A securities. Indeed, because offers will be able to be made to the public, the information on private trading systems for Rule 144A

[273] *See* letters from SIFMA and FSR (Oct. 5, 2012); and IAA.

[274] *See* letters from Consumer Federation; Fund Democracy.

[275] The use of any of the specified methods is optional. We expect that many issuers will conduct Rule 506(c) offerings in reliance on the principles-based method of verification, in light of its flexibility and efficiency.

securities could be made available to all investors, even though sales would be limited to QIBs.[276] In addition, currently there is no public dissemination through Trade Reporting and Compliance Engine (''TRACE'') of transactions in Rule 144A securities.[277] Now that Rule 144A is being amended to permit offers to be made to persons other than QIBs, transaction information with respect to Rule 144A securities can be publicly disseminated. Such improvements in the information available to potential investors could enhance efficiency in the Rule 144A market.

F. Additional Information Collection and Disclosures

We are amending Form D to add a new check box in Item 6 of Form D that will require an issuer to indicate whether it is relying on Rule 506(c) in conducting its offering. With this information, the Commission will be able to more effectively analyze the use of Rule 506(c). The marginal cost to issuers of providing this information is likely to be low because Form D already requires issuers to identify the exemption on which they are relying. Commenters generally supported the proposal to have a new check box in Item 6 of Form D as a way to identify Rule 506(c) offerings.[278] One commenter, however, questioned the usefulness of the information provided by the new check box.[279]

Much of what we know about the size and characteristics of the private offering market comes from Form D filings. The information collected to date and described in this release illustrates and underscores the importance of the private offering market to the U.S. economy. The continued collection of this information following the elimination of the prohibition against general solicitation in Rule 506(c) and Rule 144A offerings will be an important tool in assessing the ongoing economic impact of the new rule amendments.

VII. Final Regulatory Flexibility Analysis

This Final Regulatory Flexibility Analysis (''FRFA'') has been prepared in accordance with Section 603 of the Regulatory Flexibility Act.[280] It relates to the amendments to Rules 500, 501, 502 and 506 of Regulation D, Form D and Rule 144A that we are adopting in this release. An Initial Regulatory Flexibility Analysis (''IRFA'') was prepared in accordance with the Regulatory Flexibility Act and included in the Proposing Release.

A. Reasons for, and Objectives of, the Action

The primary reason for, and objective of, the amendments to Rule 502 and Rule 506 is to implement the statutory requirements of Section 201(a)(1) of the JOBS Act, which directs the Commission to revise Rule 506 to provide that the prohibition against general solicitation in Rule 502(c) shall not apply to offers and sales of securities made pursuant to Rule 506, provided that all purchasers of the securities are accredited investors. Consistent with the language in Section 201(a), the amendment to Rule 506 requires issuers to take reasonable steps to verify that purchasers in any Rule 506 offering using general solicitation are accredited investors. The primary reason for, and objective of, the amendment to Form D is to assist our efforts to analyze the use of general solicitation in Rule 506(c) offerings and the size of this offering market.

The primary reason for, and objective of, the final amendment to Rule 144A is to implement the statutory requirements of Section 201(a)(2) of the JOBS Act, which directs the Commission to revise Rule 144A(d)(1) to provide that securities sold pursuant to Rule 144A may be offered to persons other than QIBs, including by means of general solicitation, provided that securities are sold only to persons that the seller and any person acting on behalf of the seller reasonably believe are QIBs.

B. Significant Issues Raised by Public Comments

In the Proposing Release, we requested comment on any aspect of the IRFA, including the number of small entities that would be subject to the proposed rule and form amendments and the nature of the effects of the proposed amendments on small entities. We received one comment addressing the IRFA.[281] This commenter stated that the Commission failed in its IRFA to consider the alternative of eliminating Form D or significantly reducing the scope of information required to be disclosed on Form D. As Form D provides meaningful information about the Regulation D market, and our need for information about this market will only increase once Rule 506(c) is in effect, we are not considering eliminating Form D or significantly reducing the scope of information required to be disclosed on Form D.

C. Small Entities Subject to the Final Rule and Form Amendments

For purposes of the Regulatory Flexibility Act, under our rules, an issuer, other than an investment company, is a ''small business'' or ''small organization'' if it has total assets of $5 million or less as of the end of its most recent fiscal year and is engaged or proposing to engage in an offering of securities which does not exceed $5 million.[282] For purposes of the Regulatory Flexibility Act, an investment company is a small entity if it, together with other investment companies in the same group of related investment companies, has net assets of $50 million or less as of the end of its most recent fiscal year.[283]

Rule 506(c) will affect small issuers (including both operating businesses and investment funds that raise capital under Rule 506) relying on this exemption from Securities Act registration. All issuers that sell securities in reliance on Regulation D are required to file a Form D with the Commission reporting the transaction. For the year ended December 31, 2012, 16,067 issuers made 18,187 new Form D filings, of which 15,208 issuers relied on the Rule 506 exemption. Based on the information reported by issuers on Form D, there were 3,958 small issuers[284] relying on the Rule 506 exemption in 2012. This number likely underestimates the actual number of small issuers relying on the Rule 506 exemption, however, because over 60% of issuers that are not pooled investment funds and over 80% of issuers that are pooled investment funds declined to report their amount of revenues in 2012.

The final amendment to Rule 144A will affect small entities that engage in

[276] Under the PORTAL Trading System developed by the Nasdaq Stock Market for trading Rule 144A securities, access is restricted to QIBs. Other privately developed Rule 144A trading systems, such as Portal Alliance, have similar restrictions.

[277] *See* FINRA Rule 6750. There is mandatory reporting of over-the-counter trades in fixed income securities. On April 19, 2013, the FINRA Board of Governors announced that it has authorized FINRA to file with the Commission ''proposed amendments to FINRA Rules 6750 and 7730 to provide for the dissemination of transactions in TRACE-eligible securities effected pursuant to Securities Act Rule 144A (Rule 144A transactions).'' *See* Letter from Richard G. Ketchum, Chairman and CEO, FINRA (Apr. 19, 2013), *available at: http://www.finra.org/Industry/Regulation/Guidance/CommunicationstoFirms/P244913*.

[278] *See* letters from MFA (Sept. 28, 2012); SIFMA and FSR (Oct. 5, 2012); IAA.

[279] *See* letter from Consumer Federation.

[280] *See* 5 U.S.C. 603.

[281] *See* letter from K. Bishop.

[282] 17 CFR 230.157.

[283] 17 CFR 270.0–10(a).

[284] Of this number, 3,627 of these issuers are not investment companies, and 331 are investment companies. We also note that issuers that are not investment companies disclose only revenues on Form D, and not total assets. Hence, we use the amount of revenues as a measure of issuer size.

Rule 144A offerings.[285] Unlike issuers that use Regulation D, issuers conducting Rule 144A offerings are not required to file any form with the Commission. This lack of data significantly limits our ability to assess the number and the size of issuers that conduct Rule 144A offerings. Still, we are able to obtain some data on non-ABS Rule 144A offerings during the 2009 to 2012 period from two commercial databases.[286] Based on these data, we identified 3,510 offerings involving 1,965 issuers from 2009 to 2012. We were able to obtain 2011 financial information for 598 of these issuers,[287] of which only 11 issuers reported total assets of less than $50 million.

D. Projected Reporting, Recordkeeping and Other Compliance Requirements

The final amendment to Rule 506 will impose certain reporting and compliance requirements on issuers that engage in general solicitation in Rule 506 offerings. As discussed above, issuers taking advantage of Rule 506(c) to engage in general solicitation in Rule 506 offerings will be required to take reasonable steps to verify that the purchasers of the securities are accredited investors. The steps required will vary with the circumstances, but we anticipate that some potential investors may have to provide more information to issuers than they currently provide, while issuers may have to apply a stricter and more costly process to verify accredited investor status than what they currently use. We expect that the costs of compliance will vary depending on the size and nature of the offering, the nature and extent of the verification methods used, and the number and nature of purchasers in the offering. Rule 506(c) does not impose any recordkeeping requirements; however, we anticipate that issuers or their verification service providers will document the steps taken to verify that purchasers are accredited investors in Rule 506 offerings involving general solicitation because the issuer has the burden of demonstrating that its offering is entitled to an exemption from the registration requirements of Section 5 of the Securities Act. To promote legal certainty, we are including in Rule 506(c) a non-exclusive list of verification methods that in and of themselves will be deemed to satisfy the verification requirement.

The final amendment to Form D will also impose an information requirement with respect to Rule 506 offerings that use general solicitation. Each issuer submitting a Form D for a Rule 506 offering will be required to check a box on the form to indicate whether the issuer is relying on the Rule 506(c) exemption. We do not believe that this revision to Form D will increase in any material way the time or information required to complete the Form D that must be filed with the Commission in connection with a Rule 506 offering.

The final amendment to Rule 144A contains no reporting, recordkeeping or compliance requirements for issuers that engage in Rule 144A offerings.

E. Duplicative, Overlapping or Conflicting Federal Rules

The Commission believes that there are no rules that duplicate, overlap or conflict with the final amendments to Rule 144A, Form D, and Rules 500, 501, 502 and 506 of Regulation D.

F. Significant Alternatives

The Regulatory Flexibility Act directs us to consider significant alternatives that would accomplish the stated objectives of our amendments, while minimizing any significant adverse impact on small entities. In regard to the final amendment to Rule 144A and the final amendment to Rule 506 to remove the prohibition against general solicitation in Rule 506 offerings where all purchasers are accredited investors and issuers have taken reasonable steps to verify purchasers' accredited investor status, there are no significant alternatives to these amendments that would accomplish the stated objectives of Section 201(a) of the JOBS Act. Eliminating the prohibition against general solicitation for a subset of Rule 506 offerings is intended to assist small entities—and other entities—seeking to raise capital. Small entities are not required to use Rule 506(c) to raise capital and would do so presumably only if it would be useful to them.

In connection with the final amendment to Form D and the final amendment to Rule 506 that requires issuers to take reasonable steps to verify that purchasers of securities are accredited investors, the Commission considered the following alternatives: (1) Establishing different compliance or reporting standards that take into account the resources available to small entities; (2) clarifying, consolidating or simplifying compliance requirements under the rule; (3) using design rather than performance standards; and (4) exempting small entities from coverage of all or part of the amendment to Rule 506.

With respect to using design rather than performance standards, we note that the ''reasonable steps to verify'' requirement in Rule 506(c) is a performance standard. We believe that the flexibility of a performance standard accommodates different types of offerings and purchasers without imposing overly burdensome methods that may be ill-suited or unnecessary to a particular offering or purchaser, given the facts and circumstances. The Commission is not adopting different compliance or reporting requirements or timetables for small entities under Rule 506(c). The particular steps necessary to meet the requirement to take reasonable steps to verify that purchasers are accredited investors will vary according to the circumstances. Different compliance requirements for small entities may create the risk that the requirements may be too prescriptive or, alternatively, insufficient to verify a purchaser's accredited investor status. Special requirements for small entities may also lead to investor confusion or reduced investor participation in Rule 506 offerings if they create the impression that small entities have a different standard of verification than other issuers of securities. As the verification requirement is intended to protect investors by limiting participation in unregistered offerings to those who are most able to bear the risk, we are of the view that a flexible standard applicable to all issuers better accomplishes the goal of investor protection that this requirement is intended to serve. At the same time, the non-exclusive list of verification methods that we are including in the final rule will provide additional legal certainty to all issuers, including small entities. The Commission is not adopting a different reporting requirement for small entities because the additional information that will be required in Form D is minimal and should not be unduly burdensome or costly for small entities.

We similarly believe that it does not appear consistent with the objective of the final amendments or the considerations described above regarding investor confusion and investor participation to further clarify, consolidate or simplify the amendments for small entities. With respect to

[285] While it may be theoretically possible for a small entity to meet one part of the definition of ''qualified institutional buyer'' (*e.g.,* an ''entity, all of the equity owners of which are qualified institutional buyers, acting for its own account or the accounts of other qualified institutional buyers''), we do not have any information to suggest that there are such small entities. Accordingly, the regulatory flexibility analysis in regard to Rule 144A is focused on small issuers that engage in Rule 144A offerings.

[286] These databases are Thomson Financial's SDC Platinum Service and Sagient Research System's Placement Tracker database.

[287] Financial data for fiscal year 2011 was obtained from Compustat, a product of Standard and Poor's.

exempting small entities from coverage of these final amendments, we believe such an approach would be contrary to the requirements of, and the legislative intent behind, Section 201(a) of the JOBS Act, as evidenced by the plain language of the statute.

VIII. Statutory Authority and Text of Final Rule and Form Amendments

The final amendments contained in this release are being adopted under the authority set forth in Sections 4(a)(1), 4(a)(2), 7, 17(a), 19 and 28 of the Securities Act, as amended, Sections 2, 3, 9(a), 10, 11A(c), 12, 13, 14, 15(c), 15(g), 17(a), 23(a) and 30 of the Exchange Act, as amended, Sections 23, 30 and 38 of the Investment Company Act, as amended, and Section 201(a) of the JOBS Act.[288]

List of Subjects in 17 CFR Parts 230, 239 and 242

Reporting and recordkeeping requirements, Securities.

For the reasons set out above, the Commission is amending Title 17, chapter II of the Code of Federal Regulations, as follows:

PART 230—GENERAL RULES AND REGULATIONS, SECURITIES ACT OF 1933

■ 1. The general authority citation for Part 230 is revised to read as follows:

Authority: 15 U.S.C. 77b, 77b note, 77c, 77d, 77d note, 77f, 77g, 77h, 77j, 77r, 77s, 77z-3, 77sss, 78c, 78d, 78j, 78*l,* 78m, 78n, 78*o,* 78*o*-7 note, 78t, 78w, 78*ll* (d), 78mm, 80a-8, 80a-24, 80a-28, 80a-29, 80a-30, and 80a-37, and Pub. L. 112–106, sec. 201(a), 126 Stat. 313 (2012), unless otherwise noted.

* * * * *

§ 230.144A [Amended]

■ 2. Amend § 230.144A by:

■ a. In Preliminary Note 7, removing the reference to ''section 4(2)'' and adding in its place ''section 4(a)(2)'';

■ b. In paragraph (a)(1)(i)(A), removing the reference to ''section 2(13)'' and adding in its place ''section 2(a)(13)'';

■ c. In paragraph (b), removing the reference to ''sections 2(11) and 4(1)'' and adding in its place ''sections 2(a)(11) and 4(a)(1)'';

■ d. In paragraph (c), removing the references to ''section 4(3)(C)'', ''section 2(11)'' and ''section 4(3)(A)'' and adding in their place ''section 4(a)(3)(C)'', ''section 2(a)(11)'' and ''section 4(a)(3)(A),'' respectively;

■ e. In paragraph (d)(1), first sentence, removing the phrase ''offered or''; and

■ f. In paragraph (d)(1), first sentence, removing the phrase ''an offeree or'' and adding in its place ''a''.

§ 230.500(c) [Amended]

■ 3. Amend § 230.500(c) by:

■ a. Removing the reference to ''section 4(2)'' and adding in its place ''section 4(a)(2)''; and

■ b. In the second sentence, adding ''(b)'' after ''rule 506'' and after ''(§ 230.506''.

§ 230.501 [Amended]

■ 4. Amend § 230.501 by:

■ a. In paragraph (a)(1), removing the reference to ''section 2(13)'' and adding in its place ''section 2(a)(13)''; and

■ b. In paragraph (g), removing the reference to ''section 2(4)'' and adding in its place ''section 2(a)(4)''.

§ 230.502 [Amended]

■ 5. Amend § 230.502 by:

■ a. In paragraphs (b)(1), (b)(2)(iv), (b)(2)(v) and (b)(2)(vii), removing the reference to ''§ 230.506'' and adding in its place ''§ 230.506(b)'';

■ b. In paragraph (c), first sentence, adding the phrase ''or § 230.506(c)'' after the phrase ''Except as provided in § 230.504(b)(1)'';

■ c. In paragraph (d), removing the reference to ''section 4(2)'' and adding in its place ''section 4(a)(2)''; and

■ d. In paragraph (d), removing the reference to ''section 2(11)'' and adding in its place ''section 2(a)(11).''

■ 6. Amend § 230.506 by:

■ a. In paragraph (a), adding the phrase ''or (c)'' after the phrase ''satisfy the conditions in paragraph (b)'';

■ b. In paragraph (a), removing the phrase ''section 4(2)'' and adding in its place ''section 4(a)(2)'';

■ c. In the heading of paragraph (b), adding the phrase ''*in offerings subject to limitation on manner of offering''* after the phrase ''*Conditions to be met'';*

■ d. In the note following paragraph (b)(2)(i), removing the phrase ''this section'' and adding in its place ''paragraph (b) of this section''; and

■ e. Adding paragraph (c) to read as follows:

§ 230.506 Exemption for limited offers and sales without regard to dollar amount of offering.

* * * * *

(c) *Conditions to be met in offerings not subject to limitation on manner of offering*—(1) *General conditions.* To qualify for exemption under this section, sales must satisfy all the terms and conditions of §§ 230.501 and 230.502(a) and (d).

(2) *Specific conditions*—(i) *Nature of purchasers.* All purchasers of securities sold in any offering under paragraph (c) of this section are accredited investors.

(ii) *Verification of accredited investor status.* The issuer shall take reasonable steps to verify that purchasers of securities sold in any offering under paragraph (c) of this section are accredited investors. The issuer shall be deemed to take reasonable steps to verify if the issuer uses, at its option, one of the following non-exclusive and non-mandatory methods of verifying that a natural person who purchases securities in such offering is an accredited investor; provided, however, that the issuer does not have knowledge that such person is not an accredited investor:

(A) In regard to whether the purchaser is an accredited investor on the basis of income, reviewing any Internal Revenue Service form that reports the purchaser's income for the two most recent years (including, but not limited to, Form W–2, Form 1099, Schedule K–1 to Form 1065, and Form 1040) and obtaining a written representation from the purchaser that he or she has a reasonable expectation of reaching the income level necessary to qualify as an accredited investor during the current year;

(B) In regard to whether the purchaser is an accredited investor on the basis of net worth, reviewing one or more of the following types of documentation dated within the prior three months and obtaining a written representation from the purchaser that all liabilities necessary to make a determination of net worth have been disclosed:

(*1*) With respect to assets: Bank statements, brokerage statements and other statements of securities holdings, certificates of deposit, tax assessments, and appraisal reports issued by independent third parties; and

(*2*) With respect to liabilities: A consumer report from at least one of the nationwide consumer reporting agencies; or

(C) Obtaining a written confirmation from one of the following persons or entities that such person or entity has taken reasonable steps to verify that the purchaser is an accredited investor within the prior three months and has determined that such purchaser is an accredited investor:

(*1*) A registered broker-dealer;

(*2*) An investment adviser registered with the Securities and Exchange Commission;

(*3*) A licensed attorney who is in good standing under the laws of the

[288] Although 15 U.S.C. 77d note is not an authority for the amendments in this release, it is being included in the instruction below for the general authority citation for Part 230 to ensure that the Code of Federal Regulations is correctly updated for purposes of the bad actor disqualification rule for Rule 506 offerings also published today. *See* Bad Actor Release.

jurisdictions in which he or she is admitted to practice law; or

(*4*) A certified public accountant who is duly registered and in good standing under the laws of the place of his or her residence or principal office.

(D) In regard to any person who purchased securities in an issuer's Rule 506(b) offering as an accredited investor prior to September 23, 2013 and continues to hold such securities, for the same issuer's Rule 506(c) offering, obtaining a certification by such person at the time of sale that he or she qualifies as an accredited investor.

Instructions to paragraph (c)(2)(ii)(A) through (D) of this section:

1. The issuer is not required to use any of these methods in verifying the accredited investor status of natural persons who are purchasers. These methods are examples of the types of non-exclusive and non-mandatory methods that satisfy the verification requirement in § 230.506(c)(2)(ii).

2. In the case of a person who qualifies as an accredited investor based on joint income with that person's spouse, the issuer would be deemed to satisfy the verification requirement in § 230.506(c)(2)(ii)(A) by reviewing copies of Internal Revenue Service forms that report income for the two most recent years in regard to, and obtaining written representations from, both the person and the spouse.

3. In the case of a person who qualifies as an accredited investor based on joint net worth with that person's spouse, the issuer would be deemed to satisfy the verification requirement in § 230.506(c)(2)(ii)(B) by reviewing such documentation in regard to, and obtaining written representations from, both the person and the spouse.

PART 239—FORMS PRESCRIBED UNDER THE SECURITIES ACT OF 1933

■ 7. The authority citation for Part 239 continues to read, in part, as follows:

Authority: 15 U.S.C. 77f, 77g, 77h, 77j, 77s, 77z–2, 77z–3, 77sss, 78c, 78*l,* 78m, 78n, 78*o* (d), 78o–7 note, 78u–5, 78w(a), 78*ll,* 78mm, 80a–2(a), 80a–3, 80a–8, 80a–9, 80a–10, 80a–13, 80a–24, 80a–26, 80a–29, 80a–30, and 80a–37, unless otherwise noted.

■ 8. Amend Form D (referenced in § 239.500) by:

■ a. In Item 6, removing the phrase ''Rule 506'' and adding in its place ''Rule 506(b)'' next to the appropriate check box, and removing the phrase ''Securities Act Section 4(5)'' and adding in its place ''Securities Act Section 4(a)(5)'' next to the appropriate check box;

■ b. In Item 6, adding a check box that reads ''Rule 506(c)'' after the newly redesignated Rule 506(b) check box; and

■ c. In the instruction ''Who must file:'', removing the reference to ''Section 4(5)'' and adding in its place ''Section 4(a)(5).''

(**Note:** The text of Form D does not, and the amendments will not, appear in the Code of Federal Regulations.)

PART 242—REGULATIONS M, SHO, ATS, AC, AND NMS AND CUSTOMER MARGIN REQUIREMENTS FOR SECURITY FUTURES

■ 9. The authority citation for Part 242 continues to read as follows:

Authority: 15 U.S.C. 77g, 77q(a), 77s(a), 78b, 78c, 78g(c)(2), 78i(a), 78j, 78k–1(c), 78*l,* 78m, 78n, 78o(b), 78o(c), 78o(g), 78q(a), 78q(b), 78q(h), 78w(a), 78dd–1, 78mm, 80a–23, 80a–29, and 80a–37.

§ 242.101 [Amended]

■ 10. Amend § 242.101 by:

■ a. In paragraph (b)(10) introductory text, removing the phrase ''offered or''; and

■ b. In paragraph (b)(10)(i), removing the phrase ''offerees or''.

§ 242.102 [Amended]

■ 11. Amend § 242.102 by:

■ a. In paragraph (b)(7) introductory text, removing the phrase ''offered or''; and

■ b. In paragraph (b)(7)(i), removing the phrase ''offerees or''.

§ 242.104 [Amended]

■ 12. Amend § 242.104 by:

■ a. In paragraph (j)(2) introductory text, removing the phrase ''offered or''; and

■ b. In paragraph (j)(2)(i), removing the phrase ''offerees or''.

By the Commission.

Dated: July 10, 2013.

Elizabeth M. Murphy,

Secretary.

[FR Doc. 2013–16883 Filed 7–23–13; 8:45 am]

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