The Commonwealth of Massachusetts
Secretary of the Commonwealth
State House, Boston, Massachusetts 02133

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Secretary of the Commonwealth

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Submitted electronically to rule-comments@sec.gov

Elizabeth M. Murphy
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

RE: Comments in Response to S.E.C. Release "Amendments to Regulation D, Form D and Rule 156 under the Securities Act" (the "Release" or the "Proposal") Release Nos. 33-9416, 34-69960, IC-30595 (File No. S7-06-13)

Dear Ms. Murphy,

I am writing in my capacity as the chief securities regulator for Massachusetts via the administration of the Massachusetts Uniform Securities Act by the Massachusetts Securities Division (the "Division").

We appreciate that the Commission has included in the Proposal many of the comments and ideas suggested Massachusetts and other state regulators and by NASAA in the course of the Rule 506 rulemaking. The market for securities and offered and sold under the new Rule 506(c) exemption will present new opportunities and risks. As regulators, we must fulfill our missions to protect investors from fraud and abuse in this changing environment.

Introduction: The Commission Should Promote Transparency and the Distribution of Certain Basic Items of Information in Rule 506(c) Offerings

The new Rule 506(c) exemption will fundamentally change the securities markets by permitting issuers to use general solicitation and advertising to offer unregistered securities to a broad public in transactions where sales are limited to accredited investors. Many of these offerings will be highly visible because they will be posted on the Internet

and/or offered through other electronic media. The consequences of this new exemption will undoubtedly be substantial, and will likely extend beyond our ability to predict.

These offerings will have a very broad reach. Offering materials posted on the internet for a Rule 506(c) offering potentially may be seen by more investors than ever would have seen solicitation materials for a firmly-underwritten IPO in the 1980s or 1990s. Because of this broad reach, we urge the Commission to bring as much basic information and transparency as possible to this new segment of the securities market.

A key principle of the federal Securities Acts and state securities acts is to address the informational imbalance that typically exists between the sellers and purchasers of securities. While we acknowledge that Rule 506(c) transactions are not registered, it is sound and appropriate policy for the Commission to bring transparency to these markets and promote the dissemination of certain basic items of information about these offerings.

We note that some commenters on the Proposal have asked the Commission to weaken or not adopt some of the specific proposals in the Release. While the Commission must fairly consider all comments received, we urge you to stand your ground on the proposals overall. The regulations for the Rule 506(c) exemption will need to serve the interests of many constituencies, including but not limited to: small business issuers, angel investors, small retail investors, the media, securities analysts, government regulators, and academics. The Commission's rulemaking should promote transparency. This will help combat fraud, and it may promote an appropriate and beneficial sharing by market participants of information about the merits of Rule 506(c) offerings.

How Massachusetts and Other States Use Form D

We appreciate that the Proposal specifically recognizes how the states now use information in Form D filings to understand the market, to learn about issuers and offerings, and to investigate and combat fraud. In view of this, we urge that the filing of Form D must be mandatory, and the form must include the necessary items of information referenced in the Proposal.

Form D plays an important role in the Securities Division's enforcement efforts. When investors contact the Division about an unregistered offering, the Division's staff checks the Division's database and the EDGAR database for a Form D filing. Simply finding the Form D helps indicates the kind of offering it is, and the filing may give an indication that the issuer intends to comply with the rules for unregistered offerings. The items of information in the Form D are important and useful to the Division. These include the address of the issuer; the type of security being offered; the business of the issuer; information about officers and directors; and information on compensated selling persons (brokers and finders). Selling person information is particularly important to the Division, because in many cases it enables the Division to detect unregistered investment finders –a category of persons that shows up in many fraudulent and abusive offerings.

The Filing of Form D Should Be Required and There Must Be a Meaningful Enforcement of the Filing Requirement

As the Release states, many issuers claiming the Rule 506 exemption do not file Form Ds with the Commission.[1] The Form Ds that are not filed with the Commission represent a significant loss of information to potential investors, to the marketplace as a whole, and to regulators.

The states have a particular interest in Form D filings because they serve as a window into an otherwise opaque or invisible market for securities. The states' ability to receive filings for these transactions depends on the SEC receiving Form Ds from issuers using the Rule 506 exemption. Pursuant to Section 18 of the Securities Act of 1933[2], the state securities agencies may receive any notice filing for Rule 506 offerings that is based on Form D and other documents *as filed with the Commission.* If no Form D is filed with the Commission, the states also typically will not receive a filing.

The states have a strong interest in knowing about offerings that are being offered in, or being offered from, their markets. The state securities agencies are often the first regulators that investors turn to when they want information about an investment or a sponsor, or when they believe they are victims of investment fraud. When an issuer has no Form D on file with either a state or federal agency, the states often will not have even the most basic information about the offering or the people behind it. We need the information Form D filings provide to inform ourselves and investors about these offerings. Moreover, these filings provide information that helps states start investigations when fraud or other violations of the law are suspected.

The Commission should require that all Rule 506 issuers file Form Ds. To make this requirement meaningful, the Commission must establish incentives for issuers to file. The Commission's proposed 1-year bar on using the exemption for future offerings strikes an appropriate balance between the needs of issuers and the need to assure compliance with the requirements of the exemption. In response to the Commission's inquiry, we also believe it would be logical and appropriate to once again make the filing of Form D a condition of the exemption. Many (or most) other regulatory regimes work this way; for instance, in most states, one must register a motor vehicle before it can be driven on the roads. Requiring advance compliance with the notice filing requirement is reasonable.

Finally, we are concerned that a culture of non-compliance is developing with respect to filing Form D for Rule 506 offerings. It is easy to foresee that a widespread attitude

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[1] See, e.g., Release at Footnote 85

[2] See, Sections 18(b)(4)(D) and 18(c)(2)(A) of the Securities Act of 1933, "(A) Notice Filings Permitted. **Nothing in this section prohibits the securities commission (or any agency or office performing like functions) of any State from requiring the filing of <u>any document filed with the Commission</u> pursuant to this title**, together with annual or periodic reports of the value of securities sold or offered to be sold to persons located in the State (if such sales data is not included in documents filed with the Commission), solely for notice purposes and the assessment of any fee, together with a consent to service of process and any required fee." (emphasis added)

among issuers will be that: "The SEC says you are supposed to file Form D, but you really don't need to file it." Current SEC rule enforcement relating to Form D fosters such an attitude. The non-enforcement of the filing requirement may signal to some issuers that the regulators are not serious about enforcing even basic rules relating to the exemptions. This is dangerous to the continued vitality of the Form D filing requirement and is also dangerous to other important elements of securities law compliance.

Advance Filing of Form D and Filing of Final Form D

The Securities Division urges the Commission to require, as set out in the Proposal, that Form D be filed *prior* to the beginning of general solicitation for an offering. The proposed 15-day advance filing appears to be appropriate, though other, perhaps shorter, advance filing periods could also be workable.

Requiring the Form D be filed in advance will bring significant benefits to several types of market participants: (1) potential investors (who will be able to read the basic information in Form D about the offering and the issuer; also, advance posting of the Form D will permit potential investors to perform some basic diligence on the offering by confirming whether or not it has made the required regulatory filing); (2) the media and other analysts (including the web-based analysts) will be able see and work with the information included in Form D; (3) financial regulators (who will be able to check whether a particular issuer and offering appear to be acting in conformity with legal requirements); and (4) academics and other observers of the financial markets.

Some comments have urged that the required Form D information be limited or held out of the public record and/or that the filing of Form D should not be required at all. We urge the Commission not to be misdirected by such comments. Curtailment of the information that Form D would provide will create a less transparent market --a market that is harder to investigate, and will create a regulatory blind area where fraud can grow.

We also strongly support the proposal that issuers file a final Form D (a closing amendment) when an offering terminates. The information will be beneficial to all the parties that have an interest in this market. The information in the final Form D will be particularly useful to regulators because it will permit us to know which offerings are in the marketplace and which offerings are no longer being offered and sold. The information in the final Form D will also help regulators to better understand the Rule 506(c) market, particularly which offerings were successful and which were not.

Items of Information in Form D

We support the Commission's proposals to increase the items of information required in Form D and to require more detail in the form. Important information in the Proposal includes: the website address for the issuer; identities of certain control persons; use of proceeds information; types of general solicitation used; and, for pooled funds, the requirement to identify the adviser of the fund.

We applaud the Commission for including in its new "bad actor" rules the confirmation box in form D that requires the issuer to indicate that there are no "bad actors" involved in the offering.

We oppose the suggestions raised by some commenters that less information should be required or that some information should be held out of the public record. These comments are fundamentally in error because Rule 506(c) offerings will *not* be private placements. Instead, these offerings will be offered and sold using general solicitation and/or general advertising. Issuers that want to generally advertise their offerings while at the same time keeping out of the marketplace the basic information that the proposed Form D would require are unfairly trying to have things both ways. This would be detrimental to investors and the marketplace. It is entirely appropriate to require that issuers using the Rule 506(c) exemption must provide this basic information to regulators and the market.

The costs of asking issuers to complete the fill-in-the-blanks items of Form D will be modest, because the form asks for information that issuers conducting a securities offering have readily available. These modest costs pale in comparison to great benefits this information will provide to the investing public and regulators.

Required Legends in General Solicitation Materials

The Securities Division supports requiring disclosure legends to be included in general solicitation materials for Rule 506(c) transactions. The disclosure legends included in the Proposal are sound and will give disclosure that should protect many investors

At a minimum, disclosure legends on general solicitation materials should disclose that the security is being offered pursuant to Rule 506(c), that the offering is not registered under state and federal securities laws, and that there may be no market or no liquidity for the security.

We note that many commenters have objected to requiring any legend in the advertising and solicitation material. We urge that this comment is fundamentally wrong in light of the fundamental changes Rule 505(c) will bring. The longstanding general requirement of both the Securities Act of 1933 and the Investment Company Act of 1940 is that public securities offerings must be registered. Under Rule 506(c), issuers will be offering unregistered securities to a broad public. Because of this change to a decades-old rule in the securities market, it is necessary to clearly tell potential investors that these securities are not registered and that they will have different characteristics, including risk characteristics, than the registered securities they may be familiar with. Failure to provide this information would result in communications that may be misleading to investors because they omit material facts about the offering.

Disclosure legends will also be useful to state regulators. They will help us to distinguish offerings that are being made under Rule 506(c) from offerings conducted in disregard of legal requirements.

Required Disclosures by Pooled Investment Vehicles, including Hedge Funds

We strongly support the proposed requirements to make disclosure legends and the advertising practice rules Rule 156 (under the Securities Act) applicable to pooled investment vehicles such as hedge funds and private equity funds.

In the current investment market, many investors and households invest in shares of regulated investment companies.[3] The Investment Company Act and the Investment Advisors Act have helped make investment companies appropriate vehicles for many retail investors to participate in the securities markets. Privately sold funds, such as hedge funds and private equity funds, do not operate under the limitations imposed on mutual funds by the federal laws. In view of this difference, it is necessary to make it as clear as possible to retail investors the distinctions between mutual funds and often-riskier private funds. For the same reasons, we support the Commission's application of basic fund antifraud rules to public advertisements for unregistered funds.

Comments on the Revision of the Definition of Individual Accredited Investors

In response to the Commission's request for comments on the accredited investor definition in Regulation D, we restate our past comments that the financial standards for individuals to be accredited must be significantly raised in order to protect retail investors.

We are particularly concerned that the standard that defines an individual as accredited based on a net worth of $1 million (excluding the value of the principal residence) creates significant risks for older investors. The Securities Division has seen in its enforcement actions[4] that many investors who qualify as accredited based on net worth alone are not investors who can fend for themselves in the financial markets. Many of these investors are savers who have built a nest egg for retirement. These investors do not necessarily have meaningful investment sophistication, and they are vulnerable under current rules to being over-concentrated in high-risk and/or illiquid investments. Any revised definition of accredited investor must take the vulnerability of these investors into account.

The Commission's Comprehensive Work Plan to Monitor the Market for Unregistered Offerings

We applaud the Commission's comprehensive work plan to monitor and study the developing public market for unregistered securities offerings, particularly under SEC Rule 506(c).

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[3] In 2012, an estimated 92 million individual investors owned mutual funds and held 89 percent of total mutual fund assets at year-end. Altogether, 53.8 million households, or 44 percent of all U.S. households owned mutual funds. Investment Company Institute, *2013 Investment Company Fact Book.*

[4] See, *e.g* , In the Matter of Securities America, Inc. Mass. Securities Division Docket No. 2009-9985 (sales of Medical Capital Notes in Rule 506 offerings)

All securities regulators will need to develop fresh approaches to the changes and challenges this new market will present. Also, as we have seen too often in the past, fraud operators are often attracted to newly deregulated areas of the market. In response to these challenges, my Office has initiated a new iCrowd Section within the Securities Division. The responsibilities of this new Section will include observing and gather information about this new market, and working to detect and prevent fraud.

We appreciate this opportunity to comment on these important issues. It is crucial to investor protection and to the health of the financial markets that the regulations adopted to implement the Rule 506(c) exemption should strike an appropriate balance between the needs of issuers that want increased access to capital and the necessity to protect investors from fraudulent and misleading offerings.

If you have questions about this letter or my Office can assist in any way, please contact me or Bryan Lantagne, Director of the Massachusetts Securities Division. Mr. Lantagne's telephone number is (617) 727-3548 and his e-mail address is bryan.lantagne@sec.state.ma.us.

Sincerely,

William Francis Galvin
Secretary of the Commonwealth
Commonwealth of Massachusetts