SIDLEY AUSTIN LLP
SIDLEY

SIDLEY AUSTIN LLP
787 SEVENTH AVENUE
NEW YORK, NY 10019
(212) 839 5300
(212) 839 5599 FAX

jmclaughlin@sidley.com
212-839-5312

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By Email: rule-comments@sec.gov

October 5, 2012

U.S. Securities and Exchange Commission
100 F Street, NE
Washington, D.C. 20549-1090
Attention: Elizabeth M. Murphy, Secretary

Re: Eliminating the Prohibition Against General Solicitation and General Advertising in Rule 506 and Rule 144A Offerings
(Rel. No. 33-9354; File No. S7-07-12)

Ladies and Gentlemen:

The Commission's proposals in SEC Release No. 33-9354 (the "Release") relating to Rule 506 must be judged in terms of whether they fulfill the Congressional mandate in Section 201(a)(1) of the JOBS Act. That mandate was to make Rule 506 private placements more efficient by eliminating the prohibition on general solicitation and general advertising ("general solicitation").

In my view, the proposals fall far short of fulfilling the Section 201(a)(1) mandate.

1. The Commission wrongly construes the "reasonable steps" element of Section 201(a)(1) as a condition to the exemption.

The first sentence of Section 201(a)(1) says that the Commission "shall revise its rules issued in section 230.506 of title 17, Code of Federal Regulations, to provide that the prohibition against general solicitation or general advertising contained in section 230.502(c) of such title shall not apply to offers and sales of securities made pursuant to section 230.506, provided that all purchasers of the securities are accredited investors."

The second sentence of Section 201(a)(1) says that "[s]uch rules [i.e., the Commission's rules issued in section 230.506] 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."

The only way to read the second sentence as imposing an additional condition to the exemption is to supply the words "and further provided" to the first sentence and to rewrite the first four words of the second sentence as "that the issuer shall ...." Such rewriting of statutes is uniformly rejected by the courts, but the Release does not even discuss the basis for the Commission's contrary application of the statute.

It should be noted that when Congress intends to require someone to have a "reasonable belief" and also to take "reasonable steps" to back up that belief, it knows how to do so. An example can be found in Section 11(b)(3) of the 1933 Act, where a person asserting a due diligence defense must have "after reasonable investigation, reasonable ground to believe ..." in the accuracy of a registration statement.

The effect of construing the "reasonable steps" element as a condition to the exemption is that an issuer may have to convince a jury that its steps were "reasonable" – even in an offering where all of the investors are actually accredited investors. It must be obvious to the Commission from its experience with Rule 175 under the 1933 Act that a safe harbor with a "reasonableness" element is not a safe harbor at all. The SEC chairman noted as much in her recent correspondence with Chairman Darrell E. Issa of the House Committee on Oversight and Government Reform.[1] For the Commission not to draw upon this experience to discuss, or even to address, whether its proposed Rule 506(c) would accomplish the legislative purpose is a serious deficiency in the Release's economic analysis and its effect on small business.

2. The Commission's emphasis in the Release on the "reasonable steps" to be taken by *issuers* will have the effect of persuading issuers not to rely on proposed Rule 506(c).

Of course, Rule 506 is an issuer's exemption. But the Release almost completely ignores the fact that in a broad range of Rule 506 transactions the issuer relies on a broker-dealer to identify investors as accredited investors. (Specifically, the release refers 33 times to an issuer's reasonable belief or to various means by which an issuer may form a reasonable belief and only five times to the possibility that an issuer will rely on a broker-dealer for this purpose.) The Release thus implies that it is the issuer that will have to make use of the list of suggested methods by which to form a reasonable belief, e.g., read investors' tax returns or W-2's. Any issuer taking the Release at face value will be reluctant to rely on Rule 506(c).

The Commission should therefore acknowledge the legitimacy of the current widespread reliance by issuers on broker-dealers and, as discussed in the next section, deem such reliance to constitute "reasonable steps."

3. The statute requires the Commission to specify at least some methods that will constitute "reasonable steps," and reliance on a registered broker-dealer should conclusively be deemed to constitute "reasonable steps."

[1] "Notwithstanding the availability of a safe harbor under Rule 175 ..., it is my understanding that companies rarely include projections or earnings guidance in the prospectus." Letter from Hon. Mary L. Schapiro to Hon. Darrell E. Issa, August 23, 2012 at 18.

Section 201(a)(1) states that Rule 506 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." The reference to methods "determined" by the Commission is instructive: the statute does not refer to methods as "suggested" or "recommended" by the Commission or even to such methods as the Commission might deem relevant based on the "facts and circumstances" of a transaction. It is therefore logical to infer that the statute requires the Commission to specify at least some methods that will constitute "reasonable steps."

The Release states that the Commission is concerned that a non-exclusive list of specified verification methods "could be viewed by market participants as the required verification methods," thus leading to inflexibility. But there are many examples of Commission rules that set forth non-exclusive safe harbors, including the anti-underwriter precautions enumerated not very far away in Rule 502(d).

One such non-exclusive safe harbor should be an issuer's reliance on a registered broker-dealer. The Release acknowledges that an issuer should be entitled to rely to some degree on a list of investors "created and maintained by a reasonably reliable third party, such as a registered broker-dealer," but it fails to acknowledge the widespread practice to this effect. It also fails to acknowledge that broker-dealers are subject to their own liabilities under Section 12(a)(1), to their own responsibilities under "know your customer" rules and anti-money laundering mandates and to inspections and examinations by the Commission and other regulators. The final rule should state that an issuer will be deemed to have taken "reasonable steps" if it has relied on a registered broker-dealer to verify that investors are accredited investors, and any qualification should be limited to an issuer's having "reason to know" that such reliance is not justified.

4. Section 201(a)(1) does not authorize the Commission to adopt a separate exemption for Rule 506 offerings that use general solicitation.

Section 201(a)(1) states that the Commission shall revise "its rules issued in section 230.506 of title 17, Code of Federal Regulations, to provide that the prohibition against general solicitation or general advertising contained in section 230.502(c) of such title shall not apply to offers and sales of securities made pursuant to section 230.506, provided that all purchasers of the securities are accredited investors."

Section 201(a)(1) is clearly referring to the single set of rules embodied in Rule 506 and is clearly instructing the Commission to revise that single set of rules to exclude the applicability of the Rule 502(c) prohibition against general solicitation. There 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 and thus undermine Congress' intent to increase the efficiency of Rule 506 offerings.

5. Section 201(a)(1) does not authorize the Commission to excuse issuers from the "reasonable steps" requirement because they choose not to engage in general solicitation.

The Commission states in the Release that issuers may choose not to engage in general solicitation because they do not wish to "become subject to the new requirement to take reasonable steps to verify the accredited investor status of purchasers ...."

But the second sentence of Section 201(a)(1) states that Rule 506, as revised pursuant to the statutory mandate, "shall require the issuer to take reasonable steps ...." It does not state that such reasonable steps are not necessary just because the issuer chooses not to engage in general solicitation. The Commission's proposal, which seems designed to induce issuers to forsake the use of general solicitation in exchange for not having to engage in "reasonable steps," is therefore not authorized by the statute.

6. 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.

Section 201(a) instructs the Commission to revise Rule 506 so as to make inapplicable the Rule 502(c) prohibition on general solicitation. It does not authorize the Commission to impose burdens – such as the Form D check box – on an issuer's reliance on Rule 506 as revised in accordance with the statute.

* * *

The Commission has chosen in the Release to construe Section 201(a)(1) in ways that are not consistent with the Congressional intent. It should revise its proposals or, at the least, explain how it believes its proposals are consistent with the statute.

This letter represents my personal views and not necessarily those of my firm, its partners or its clients.

Very truly yours,

Joseph McLaughlin