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Business Law Section
Securities Regulation Committee

October 12, 2012

Securities and Exchange Commission
100 F Street, NE
Washington, D.C. 20549-1090

Submitted electronically to: rule-comments@sec.gov

Attention: Elizabeth M. Murphy, Secretary

RE: File No. S7-07-12
Eliminating the Prohibition Against General Solicitation and General Advertising in Rule 506 and Rule 144A
Release No. 33-9354

Ladies and Gentlemen:

The Securities Regulation Committee of the Business Law Section of the New York State Bar Association (the "**Committee**") appreciates the invitation from the Securities and Exchange Commission (the "**Commission**" or the "**SEC**") in Securities Act Release No. 33-9354[1] to comment on the Commission's proposed amendments to Rule 506 and Rule 144A under the Securities Act of 1933, as amended to implement Section 201(a) of the Jumpstart Our Business Startups Act (the "**JOBS Act**").

The Committee is composed of members of the New York State Bar Association, a principal part of whose practice is in securities regulation. The Committee includes lawyers in private practice and corporation law departments. A draft of this letter was reviewed by certain members of the Committee. The views expressed in this letter are generally consistent with those of the majority of members who reviewed and commented on the letter in draft form. The views set forth in this letter, however, do not necessarily reflect the views of the organizations with which its members are associated, the New York State Bar Association or its Business Law Section.

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[1] Eliminating the Prohibition Against General Solicitation and General Advertising in Rule 506 and Rule 144A Offerings Securities Act Release No. 33-9354 (Aug. 29, 2012) (hereinafter, the "Proposing Release"), *available at* http://sec.gov/rules/proposed/2012/33-9354.pdf.

A. Background

We applaud the Commission for its reasonable and flexible approach with respect to verification standards under Rule 506 and Rule 144A. The discussion in the Proposing Release of the factors that an issuer may take into account in meeting proposed Rule 506(c)'s requirement that issuers "'take reasonable steps to verify' that purchasers of the offered securities are accredited investors" is particularly helpful. We believe that discussion should provide issuers with a practical framework for making assessments. And we agree that it would be impractical to require issuers to use a specified method of verification when there are numerous ways in which an issuer can be found to have taken reasonable steps given the specific facts of a particular offering. The Proposing Release sensibly underscores that where, after consideration of the particular facts and circumstances, it appears likely that a person qualifies as an accredited investor, an issuer would have to take fewer steps to verify that status but, correspondingly, would have to take a more intensive examination when it is less clear on the face of the facts that the investor is an accredited investor. The example given, that an issuer who knows little about a potential purchaser but who sets a high minimum investment requirement might reasonably take no further steps other than to confirm that the purchaser's cash investment is not being financed by the issuer or by a third party, is useful. The entirety of the discussion in the Proposing Release, together with the detailed footnotes, should provide issuers in most instances with the ability to implement a reasonable, and reasonably efficient verification process.

We also support the Commission's determination that a privately offered fund's reliance on the Section 3(c)(1) or Section 3(c)(7) exclusions from the definition of "investment company" under the Investment Company Act of 1940, as amended, which preclude public offerings of an issuer's securities, will not be affected should a private fund wish to make a general solicitation under amended Rule 506.

In light of amended Rule 506, we address two distinct issues below: integration and transition issues and the Form D filing requirement. Finally, we suggest that given the nature of the proposed amendments, the Commission consider placing the essential elements of its guidance on Rule 506(c) on its website.

B. Transition and Integration

We expect that the amended rule will raise several integration issues, especially during the period of transition to the new rule. We request that the Commission provide further guidance on the questions below. We use the term "506(c) offering" to mean an offering in which general solicitation is used in compliance with the requirements of the amended rule.

1. <u>Converting an Offering to Accredited Investors to a 506(c) Offering</u>. An issuer conducting a Rule 506 offering to accredited investors only may wish to begin using general solicitation in a 506(c) offering after the effective date of the

proposed amendment. The issuer will have a reasonable belief that its pre-506(c) investors are accredited, but may not in every instance have taken steps to verify accredited investor status pursuant to the Commission's guidance. The issuer should not be required to close the offering for six months in order to avoid integration of the sales in the 506(c) offering with the sales made prior to the amendment. Rather, the Commission should permit the issuer to continue its Rule 506 offering under Rule 506(c), provided that all new investors in the offering meet the necessary verification standards. The issuer would then be required under Rule 503 to amend its Form D to check the Rule 506(c) box.

2. Converting an Offering to Non-Accredited Investors to a 506(c) Offering. This is a variation on the preceding scenario. An issuer conducting a Rule 506 offering to both accredited and non-accredited investors may wish to begin using general solicitation in a 506(c) offering after the effective date of the proposed amendment. Again, the issuer should be permitted to continue its Rule 506 offering under Rule 506(c), provided that all new investors in the offering meet the necessary verification standards. The issuer would be required under Rule 503 to amend its Form D to check the Rule 506(c) box. Investors who came into the offering prior to conversion to a 506(c) offering would not have purchased on the basis of general solicitation. The heightened investor protection concerns around purchases by persons who responded to general solicitation, which form the justification for the requirement to verify accredited investor status, would not apply to investors, accredited and non-accredited, who invested prior to the commencement of general solicitation.

3. Inadvertent General Solicitation Prior to the Effective Date. It occasionally happens that an issuer conducting or planning to conduct a private offering will inadvertently engage in advertising or general solicitation. This can happen, for instance, if the company CEO gives a widely disseminated interview in which he or she talks about the offering. One method of curing this mistake is to wait six months from the date of publication of the interview before commencing the offering. Given the clear statement of policy by Congress in the JOBS Act to enable capital raising by startup companies by permitting general solicitation in Rule 506 offerings, an issuer that has inadvertently engaged in general solicitation less than six months before the effective date of the amended rule should be permitted to commence a 506(c) offering on or after the effective date provided that (i) no sales were made to any person between the date of the inadvertent general solicitation and the effective date and (ii) all sales made following the effective date satisfy the requirements of Rule 506(c).

4. Integration with Crowdfunding Exemption. Issuers will be able to conduct offerings exempt under the Crowdfund Act (a "4(a)(6) offering") following the

effectiveness of Commission rulemaking under that Act. An issuer that has conducted a successful 4(a)(6) offering may be ready to commence a Rule 506 offering less than six months after the completion of the 4(a)(6) offering. The public dissemination of information about the 4(a)(6) offering on the crowdfunding platform may raise issues about whether there has been general solicitation close to the time of the Rule 506(c) offering. However, the presence of general solicitation in the 4(a)(6) offering should not be a concern with respect to investors in the subsequent offering if the issuer conducts a 506(c) offering within six months of the 4(a)(6) offering, since the issuer would have been able to use general solicitation in the 506(c) offering anyway. However, integration of the two offerings would be a problem if the conditions of the Rule 506(c) offering were deemed not to be satisfied because crowdfunding investors are not all accredited investors. The Commission should provide guidance that a Rule 4(a)(6) offering is not deemed to be integrated with a subsequent 506(c) offering.

C. Form D

We agree with the Commission's proposal to amend Form D to add a section where issuers can indicate that the offering is being conducted in accordance with Rule 506(c). As we read the proposed rules, issuers that have already been conducting an offering would be required, under Rule 503, to amend their previously filed Form Ds, if and when they determine to convert an existing Rule 506 offering to a 506(c) offering.

We believe strongly that Rule 506 should not be amended to make it a condition to the Rule 506(c) exemption that the issuer file a Form D indicating that the offering is being conducted pursuant to Rule 506(c). The consequences of losing the exemption are significantly out of proportion to the harm of failure to make the filing. An issuer that loses its Rule 506 exemption as a result of failure to file a Form D is subject not only to the penalties of failure to register under the Securities Act of 1933, as amended (the "**Securities Act**"), but also to penalties for failure to register under the securities laws of every state in which the securities were sold, because the issuer will have lost the benefit of preemption provided by Section 18 of the Securities Act. This, in turn, could have harmful effects not only on the issuer and its principals, but on investors in the issuer, if there are not sufficient funds remaining in the enterprise to repay their investments. Since the consequences of failure to register are not dependent on the merits of the offering or issuer, such a penalty could result in the failure of an otherwise sound business which seems to us to be at odds with the Congressional intent behind the JOBS Act.

D. Making Guidance Available on SEC Website

The guidance the Commission provides in its rulemaking release is extremely helpful to startup companies and other Rule 506 issuers. Because of the special interest of entrepreneurs

and others in offerings under Rule 506(c) for new businesses, we urge the Commission to place the essential elements of its guidance on Rule 506(c) on its website.

We are grateful for the opportunity to provide these comments on the Proposed Rules and for the Commission's attention and consideration. We hope that our comments, observations, and recommendations contribute to the important work of the Commission in carrying out the regulatory mandates of the JOBS Act. We would be happy to discuss these comments further with the Staff.

Respectfully submitted,

SECURITIES REGULATION COMMITTEE

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