

1 November 2012

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

Re: Eliminating the Prohibition against General Solicitation and General Advertising in Rule 506 and Rule 144A Offerings

Dear Ms. Murphy:

CFA Institute¹ appreciates the opportunity to comment on the SEC's proposal to implement certain provisions of the Jumpstart Our Business Startups Act (the "Act") that was recently enacted by Congress. Having commented previously that the Act raises a number of investor protection issues,² we welcome the opportunity to provide additional input as the SEC considers the content of these implementing regulations.

CFA Institute represents the views of investment professionals before standard setters, regulatory authorities, and legislative bodies worldwide on issues that affect the practice of financial analysis and investment management, education and licensing requirements for investment professionals, and on issues that affect the efficiency, integrity and accountability of global financial markets.

Executive Summary

CFA Institute has previously registered strong concerns that the Act will increase the possibility for fraud through provisions that reduce transparency, negate existing conflicts of interest safeguards, and significantly reduce important investor protections. We continue to hold those concerns.

Full Public Consultation and Cost Benefit Review

We applaud the SEC for issuing this proposal for public comment, rather than adopting an interim rule, despite Congressional pressure to do otherwise. Providing the public the opportunity to comment on changes to existing regulations that directly implicate investor protections was needed and appropriate under the SEC's mandate.

¹ CFA Institute is a global, not-for-profit professional association of more than 118,000 investment analysts, advisers, portfolio managers, and other investment professionals in 139 countries, of whom more than 109,000 hold the Chartered Financial Analyst® (CFA®) designation. The CFA Institute membership also includes 137 member societies in 59 countries and territories.

² See August 16, 2012 letter to Elizabeth M. Murphy from Kurt N. Schacht, CFA and Linda Rittenhouse re Jumpstart our Business Startups Act.

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“Surgeon General” Warning Label

We encourage the SEC to implement regulations that require emerging growth companies and crowd funding companies to spotlight for investors, the risks they are undertaking with these securities. We recommend that a “Surgeon General”-like banner be added to the face of any prospectus or offering conducted under the Act. This warning label should address key risks and provide prominent warnings about reduced transparency and investor protections.

Revised Accredited Investor Definition

We encourage the SEC to revise the current definition for “accredited investor”. While the current approach considers an individual’s net worth as criteria, a more meaningful definition would also include investment or financial sophistication on the part of the investor.

General Comments

As an overall comment, we greatly appreciate the fact that the SEC decided to seek public input, rather than issue an interim implementing rule. Given the nature of issues raised in this proposal, public input is meaningful and will hopefully provide constructive suggestions for finalizing a rule.

The provisions of the Act that this proposal seeks to implement contravene a number of conditions and investor protections that have been in effect for years. The safe harbor afforded under Rule 506 is limited and conditioned upon there not being a public solicitation, underscoring the need for unregistered offerings to be narrowly construed in order to safeguard investors from fraud and misrepresentation. The widening of this safe harbor to now allow JOBS Act companies to make offerings through general solicitation and advertising contravenes this fundamental principle.

As we have noted previously, the JOBS Act raises a number of concerns about potential future effects on market integrity, investor protections, and investor confidence. CFA Institute supports efforts to increase opportunities for small companies to access the capital markets for equity and debt funding that is reasonable and that do not potentially undermine basic tenets of the securities laws and investor protections. However, if the jobs this legislation intends to create come at the loss of investor confidence in the markets, the overall progress will be negated and markets will further suffer at a time when they need bolstering.

The average retail investor’s confidence has been severely shaken by the market turmoil that began in 2000. To fan recovery, investors must be persuaded by companies and regulators alike that they will not tolerate financial abuses, that conflicts of interest will be managed and that investor protections remain at the forefront. Rather than working toward these ends, the JOBS Act raises serious concerns in a number of fundamental areas, including the lack of safeguards on internal controls, the dilution of current mechanisms designed to help manage/mitigate the

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conflicts of interest between the research and investment banking functions of companies and the potentially reduction in disclosures called for in Regulation S-K.

We realize that the rule proposal before us does not address these areas but is limited to implementing the “general solicitation” changes under current Regulation D mandated by the JOBS Act. Thus, while having the concerns noted above, we generally limit our comments below to a discussion of the provisions raised in this proposal

We understand that Congress has imposed upon the SEC the duty to implement provisions of the JOBS Act in accordance with the legislation. We believe that the implementing regulations the SEC must create can and should address shortcomings and require conditions that do not contradict the JOBS Act law, but nonetheless may temper the Act’s potential damage.

We therefore encourage the SEC to reconsider its approach noted in the proposal to limit the implementing rules, and instead weigh a number of comments already received that urge further revisions to the definition of accredited investor, among other things. In light of some of the Act’s vulnerabilities and shortcomings, additional issues must be addressed in order to strengthen investor protections.

Discussion of Proposal

Currently, Regulation D allows unregistered offerings to be made to accredited investors (and up to 35 non-accredited investors) conditioned in part on there not being a general solicitation or public advertising of the offering. In contrast, proposed new Rule 506 (c) would allow issuers to offer and sell securities to the public through general solicitations and general advertising without having to register the offering with the SEC, as long as the purchasers are “accredited investors” and the seller has taken “reasonable steps” to verify that the purchaser is an accredited investor.³ By allowing unregistered offerings to be made to the public without the usual disclosure and other requirements for registered offerings, this proposed new rule removes a longstanding safeguard for investor protection. No longer will these unregistered offerings be subject to the type and degree of SEC review that investors expect and rely on in general solicitations.

There now is a need to balance the directive from Congress in implementing the JOBS Act with the SEC’s mandate to protect investors. We believe there are several measures the SEC can consider to achieve this goal.

³ As proposed to implement the JOBS Act, securities may also be offered to non “qualified institutional buyers” as long as they are sold only to qualified institutional buyers (QIBs) and provided the seller reasonably believes them to be QIBs.

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Express Warning

CFA Institute believes that proposed Rule 506 (c) opens the door to potential fraud, miscommunications, and erroneous information being provided to unsuspecting investors, who may not be aware that the offering has not been approved by or registered with the SEC. At a time when investor confidence is wavering we find the potential damage concerning.

In the proposing release, the SEC asks if there are other measures it should take in connection with removing the general solicitation prohibition. We believe the SEC has an opportunity in finalizing the rule to impose conditions that can make a real difference to unsuspecting investors.

In order to alert investors to the shortcomings implicit in Rule 506 (c) transactions, we strongly encourage the SEC to require a warning to be included in connection with the offer and sale of Rule 506 (c) securities. This “surgeon’s general” warning label should be prominently displayed in bold and reasonable-sized typeface on the face of any communication with the purpose of offering or soliciting interest in such securities. A requirement to use this label should apply to all such communications, whether in print or electronic form.

While we urge the SEC to fashion the required warning as it sees fit, we encourage use of something along the lines of the following:

These securities are being offered under the JOBS Act which permits exemptions from standard public company disclosure and transparency requirements. These exemptions permit offerings with significantly reduced disclosure, limited and unaudited financial information and very limited auditor review of internal controls over compliance and financial reporting. These securities are highly risky and should be purchased by investors who are skilled in analyzing such risks and are able to withstand a loss of their entire investment.

Additional Disclosures

In addition to the warning label, we recommend that the SEC require issuers to include prominent and broad disclosures within the body of their offering statements and interim financial statements alerting investors to potential risks. These disclosures should include clear statements about the higher possibility that investors could lose their entire investments given, among other things, the lack of an established trading market in the shares.

We also encourage the Commission to consider requiring issuers to provide other disclosures that would provide investors with meaningful relevant information and to use a distinct offering format, including:

- Use of a standard prospectus in which issuers would provide comparable, uniform and easy-to-understand elements of their offering;
- Disclosure of the use of proceeds;
- Disclosure of share issuance in connection with executive, director, and employee compensation;

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- Identification of all persons or entities holding more than 20% of outstanding equity; and
- Disclosure of all related-party transactions.

As the Commission addresses additional aspects of the JOBS Act, including crowdfunding provisions, and formulates implementing rules, we urge it to consider the following, with the objective of again providing investors with information that they may otherwise lack, given JOBS Act exemptions:

- Annual audits included in annual reports to shareowners;
- At least semi-annual updates of performance and financial condition;
- A requirement that all important company news be disclosed through normal, public delivery channels;
- Holding company principals liable for fraudulent representations;
- Consideration of separate exchanges for companies covered by the Act; and
- Requiring shares sold through crowdfunding to remain unregistered.

Reasonable Steps

In addressing what will qualify as an “accredited” investor, the SEC has chosen to use an approach that allows issuers great flexibility under proposed Rule 506 (c). We appreciate that the SEC has opted not to take a once-size-fits-all-approach so as to allow issuers to make offerings to a wide variety of purchasers and under varying circumstances, only having to take “reasonable steps to verify” that the purchaser is accredited. We also understand that consistent with Rule 506 offerings, the issuer will not lose its exemption should the purchaser turn out not to be accredited, as long as *reasonable steps* were taken to verify the status.

In many instances we believe that this flexibility for issuers may be appropriate. However, the risks involved in opening up this process argue against such flexibility and instead for clearer parameters from the SEC. In order to help bolster needed investor protections to these new types of offerings, we encourage the SEC to provide a clear and detailed description of what will be deemed to constitute “reasonable steps” that will satisfy the issuer’s obligation under proposed rule 506 (c).

Accredited Investor/Qualified Buyer

The SEC is clear that while it has provided some guidance relating to the determination of whether purchasers are accredited, it is not at this point proposing to revise the definition of “accredited.” We urge the Commission to reconsider this stance.

We have long held the position that individual financial worth does not necessarily equate with financial acumen. For that reason, we support a broader definition of “accredited” that does not just focus on net worth of a person but includes whether an investor is “sophisticated” in terms of investment and financial knowledge. If these offerings are to be conditioned on truly accredited

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investors, therefore, we believe this is an opportune time for the SEC to revise the accredited investor definition and thereby ensure that those without appropriate sophistication are not unwittingly harmed.

Conclusion

We believe the SEC has an opportunity in this rulemaking process to impose conditions on companies relying on the JOBS Act that will help buttress some important investor protections that the Act threatens. We thus encourage the SEC to include in its final rule mechanisms to provide warnings to investors and a change to the accredited investor definition that will more aptly ensure that these offerings are entered into by investors with the appropriate knowledge and understanding. Moreover, as the rulemaking process continues to implement other provisions of the JOBS Act, we urge adoption of the kinds of provisions described above that will further add needed investor safeguards.

Should you have any questions about our positions, please do not hesitate to contact Kurt N. Schacht, CFA at kurt.schacht@cfainstitute.org or 212.756.7728; or Linda L. Rittenhouse at linda.rittenhouse@cfainstitute.org or 434.951.5333.

Sincerely,

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