Amending an existing filing under Rule 506 of Regulation D

It is unclear whether an existing filer who is under Rule 506 of Regulation D will be allowed to amend its existing filing in order to claim an exemption under the new Rule 506(c) so that it may begin public advertising. Failing to allow existing Rule 506 of Regulation D filers to amend their filing will have the unintended result of giving a competitive advantage to new Rule 506 of Regulation D filers that is not available to existing filers. This result is neither a contemplated nor desired result in either the legislation or the comments to the legislation.

Existing filing under Rule 506 of Regulation D that has sold to no more than 35 non-accredited investors

A review of the proposed amendments to Rule 506 of Regulation D appears to create two classes of Rule 506 filers. The first class is made up of those who fall under section (b) of Rule 506 who are not allowed to make general solicitations or publicly advertise and are allowed to have up to 35 non-accredited investors. The second class is made up of those who will fall under the new proposed section (c) of Rule 506 who are allowed to publicly advertise and solicit generally and are not allowed to have any non-accredited investors. Pursuant to this understanding of the proposed amendment, existing filers under Rule 506 of Regulation D who have previously sold to no more than 35 non-accredited investors under the previously existing Rule 506 of Regulation D would be subject to a competitive disadvantage due to the proposed amendment to the existing rule. Such existing filers should be allowed into the new system provided that after amending their filing, the filing issuer sells only to accredited investors. If such a provision is not created, the same unintended effect discussed above will accrue; new filers will have a competitive advantage over existing filers in a way that is not anticipated by the legislative language.

Reasonable steps to verify that the purchasers of securities are accredited investors

The new section Rule 506(c) of Regulation D requires that issuers take "reasonable steps to verify that the purchasers of securities are accredited investors." In the SEC's request for comments, it correctly points out that what counts as "reasonable steps" may differ based upon the particular situation. Factors such as the minimum allowable investment, the reach of the general advertisement, buyer representations, and related disclosures will all be considered in determining whether the steps taken by an issuer to verify that the purchaser is an accredited are or are not reasonable. The SEC has proposed that no regulations be issued regarding the same to allow issuers maximum flexibility to determine, in the issuer's instance, what level of verification is reasonable. In light of the above, our question is whether, given broad/general advertising and a minimum investment of $5,000, would the representation attached hereto as Exhibit A from the purchaser be sufficient for the issuer to meet its obligation of demonstrating that it had acted reasonably in verifying the status of the purchaser as an accredited investor? As is pointed out in footnote 79 of the request for comments, several federal courts have held that an

issuer can rely on representations from the investor that he, she, or it is accredited as defined by the relevant securities rules. In light of those holdings which preclude an investor from seeking redress from an issuer for his, her, or its own misrepresentations, if the investor cannot hold the issuer responsible after misrepresenting his, her, or its status as accredited, it makes little sense for the SEC to impose a higher standard than exists based on the cases cited in footnote 79.

Exhibit A

Accredited Investor Verification

The federal securities laws define the term accredited investor in Rule 501 of Regulation D as:

1. **a bank, insurance company, registered investment company, business development company, or small business investment company;**
2. **an employee benefit plan, within the meaning of the Employee Retirement Income Security Act, if a bank, insurance company, or registered investment adviser makes the investment decisions, or if the plan has total assets in excess of $5 million;**
3. **a charitable organization, corporation, or partnership with assets exceeding $5 million;**
4. **a director, executive officer, or general partner of the company selling the securities;**
5. **a business in which all the equity owners are accredited investors;**
6. **a natural person who has individual net worth, or joint net worth with the person's spouse, that exceeds $1 million at the time of the purchase, excluding the value of the primary residence of such person;**
7. **a natural person with income exceeding $200,000 in each of the two most recent years or joint income with a spouse exceeding $300,000 for those years and a reasonable expectation of the same income level in the current year; or**
8. **a trust with assets in excess of $5 million, not formed to acquire the securities offered, whose purchases a sophisticated person makes.**

I represent and warrant that I have read and understood the above definition of accredited investor, that I am an accredited investor as such term is defined above, and that my affirmation herein may be relied upon by the issuer.