ANGEL CAPITAL ASSOCIATION

August 16, 2011

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

Re: File Number S7-21-11
Disqualification of "Bad Actors" from Rule 506 Offerings

Dear Ms. Murphy:

We want to thank staff of the Commission's Office of Small Business Policy for arranging a July 23rd teleconference with the Angel Capital Association to discuss our prior letter to you on this subject. We also appreciate their invitation to follow up with additional thoughts, in light of that discussion. This letter sets forth those additional thoughts.

We want to again emphasize how much we endorse what Section 926 of the Dodd-Frank Act attempts to achieve, as well as the Commission's goal to disqualify from Regulation D exemptions generally those offerings that knowingly employ "bad actors." There is a sentence at page 58 of the Commission's release announcing the proposed rule that expresses our best hopes for this regulatory reform: to "increase investor trust in the integrity of the private placement and small offering markets (which could contribute to a lower cost of capital for issuers)."

The most important point we discussed during the teleconference concerned footnote 86 of the release, and in particular the sentence of the proposed instruction the footnote references, which reads, "The nature and scope of the requisite inquiry [of an issuer, as to whether a "bad actor" is participating in an offering] will vary based on the circumstances of the issuer and the other offering participants."

We have no problem with that proposed instruction. But we continue to have concerns with the actual language in the proposed regulatory safe harbor itself: "If the issuer establishes that it did not know, and in the exercise of reasonable care could not have known, that a disqualification existed . . ." We think the language is confusing and arguably inhospitable to the concept of a "sliding scale" of care in the circumstances.

It is ironic that our principal stumbling block is the safe harbor; we know the staff intended it to be an additional comfort to small issuers, and not an impediment. Be that as it may, we continue to feel that the language conflates a reasonableness or "due inquiry" standard ("the exercise of reasonable care") with a far more stringent standard, almost approaching strict liability ("could not have known").

Perhaps the Commission's intentions would be better served by rewording the proposed safe harbor as follows: "If the issuer establishes, after inquiry that is reasonable in the particular

circumstances, that it did not know that a disqualification existed." This regulatory language should be supplemented with an instruction that, where an issuer engages no compensated solicitor but instead sells securities directly in conformance with the exemption, the use of questionnaires (as proposed in our letter dated July 14, 2011) will ordinarily satisfy the standard.

Finally, to further amplify the kind of adjustments in the proposed rule and Commission guidance that we request in order to protect the viability of Rule 506 for startups and angel investing, enclosed with this letter is a "redline" of the last paragraph on page 42 of the release. It may be that we are on the same page with the staff as to intent, but we don't think the language in the proposed rule is as flexible as the concepts we discussed in the teleconference - concepts which, admittedly, are well reflected elsewhere in the release.

Sincerely,

Sincerely,

Marianne Hudson
Executive Director

Enclosure: Suggested guidance on "reasonable care" standard

Enclosure to ACA letter to SEC dated August __, 2011

Suggested language for the "safe harbor" rule itself:

(2) Paragraph (c)(1) of this section shall not apply:

. . .

(ii) If the issuer establishes, after inquiry that is reasonable in the particular circumstances, that it did not know that a disqualification existed.

Suggested guidance on "reasonable care" standard for issuers with regard to "bad actors":

The following text is an adaptation of the last paragraph on page 42 of SEC Release No. 33-9211; File No. S7-21-11, "Disqualification of Felons and Other 'Bad Actors' from Rule 506 Offerings." The redlining indicates how the Commission's approach could be modified to address the ACA's concerns. As so modified, we think this paragraph would be good guidance to publish with the final "bad actor" disqualification rule.

The steps an issuer should take to exercise reasonable care would vary according to the circumstances of the covered persons and the offering, taking into account such factors as the risk that bad actors could be present, the presence of other screening and compliance mechanisms and the cost and burden of the inquiry. In ~~some~~ circumstances where the issuer does not engage a compensated solicitor, factual inquiry of the covered persons themselves (for example, by including additional questions in questionnaires issuers may already be using to support disclosures regarding directors, officers and significant shareholders of the issuer) ~~may be adequate. Issuers~~should ordinarily be adequate. In circumstances where the issuer does engage a compensated solicitor, a response by the compensated solicitor to the issuer's factual inquiry, accompanied by an affidavit that the compensated solicitor's response is correct and may be relied upon, should ordinarily be adequate. Where persons solicited for information are not responsive, issuers should also consider whether investigating publicly available databases is reasonable. ~~In some circumstances~~Where factual inquiry yields inconsistent information, further steps may be necessary.

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