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October 4, 2011

U.S. Securities and Exchange Commission
100 F Street, N.E.
Washington, DC 20549-1090
Attention: Elizabeth M. Murphy, Secretary

Re: File No. S7-21-11
Release No. 33-9211
Disqualification of Felons and Other "Bad Actors" From Rule 506 Offerings

Ladies and Gentlemen:

This letter is submitted on behalf of the Federal Regulation of Securities Committee, the Middle Market and Small Business Committee, the State Regulation of Securities Committee and the Private Equity and Venture Capital Committee (the "***Committees***" or "***we***") of the Business Law Section (the "***Section***") of the American Bar Association ("***ABA***") in response to the request by the U.S. Securities and Exchange Commission (the "***Commission***") for comments on its May 25, 2011 proposing release referenced above (the "***Proposing Release***"). The comments expressed in this letter represent the views of the Committees only and have not been approved by the ABA's House of Delegates or Board of Governors and therefore do not represent the official position of the ABA. In addition, this letter does not represent the official position of the Section.

I. Overview

We appreciate the opportunity that the Commission has afforded us to comment on these proposed rules. Section 926 ("***Section 926***") of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the "***Dodd-Frank Act***") mandated that the Commission adopt rules that disqualify securities offerings involving certain "felons and other 'bad actors'" from reliance on the safe harbor from registration under Section 4(2) of the Securities Act of 1933, as amended (the "***Securities Act***") provided by Rule 506 ("***Rule 506***") of Regulation D ("***Regulation D***") under the Securities Act.

We recognize that Section 926 requires that the Commission's rules must be "substantially similar" to Rule 262 ("***Rule 262***") of Regulation A ("***Regulation A***") under the Securities Act, which is the analogous disqualification provision of Regulation A, and that the Commission must also implement by its rulemaking additional provisions contemplated by Section 926. Although we understand the constraints on the Commission's discretion in connection with the implementation of Section 926, in this letter we suggest several areas where the Commission should consider adjusting its approach to such implementation. In this regard, we believe that the current rulemaking

prompted by the Dodd-Frank Act offers an opportunity to provide uniformity in the "bad actor" disqualification provisions that are applicable to regulatory safe harbors for unrestricted securities offerings, while at the same time addressing those portions of Rule 262 that are now outdated and do not necessarily conform to the contemplated scope of the Rule 506 disqualification provision. While we fully recognize the laudable goal of promoting investor protection by disqualifying those securities offerings in which a felon or other "bad actor" is involved, we are particularly concerned that an overly broad implementation of the Section 926 directive could undermine the utility of Rule 506 as the most widely used exemptive safe harbor for private placements of securities, thereby materially and adversely affecting the ability of many companies, including many private companies and smaller reporting companies, to obtain capital.

We recognize that Section 926 mandates disqualification in specified circumstances. In other circumstances under the Commission's consideration, however, we believe that a disclosure approach may be more effective than a disqualification approach in protecting investors. Such a disclosure approach would be less draconian in its impact on issuers and market participants, and more flexible and cost-effective in addressing particular circumstances, as discussed below. In some circumstances issuers and market participants can proactively adjust their management or staffing to address investor protection concerns, without being obligated to forgo the Rule 506 safe harbor or necessitating an issuer's reliance upon different exemptions bearing higher compliance costs or requiring the issuer to incur the costs and burdens of a full securities registration. The lack of availability of Rule 506 may thus work to the detriment of all investors of the issuer. In the worst case scenario, a post-offering determination that Rule 506 was not available for the offering would constitute a registration violation and trigger related rescission rights for all purchasers in the offering, a draconian remedy when compared to the antifraud remedies attendant to a failure to disclose the involvement of certain felons and bad actors in an offering. Prescribed self-disclosure as a condition to avoiding the disqualification could serve as an appropriate method of addressing investor protection concerns without disqualifying the entire offering. For example, in the context of investment adviser regulation, the Commission requires disclosure of specified legal and disciplinary events in Item 9. *Disciplinary Information* of Form ADV, Part 2A, and Item 3, *Disciplinary Information*, of Part 2B.[1] This approach assures that prospective clients of the investment adviser receive this important background information in connection with their investment-related decision-making, but does not preclude the investment-related services from being offered or performed by the firm and allows the prospective client to assess the circumstances and related risks. We believe a similar disclosure-based system would be of equal merit in the Rule 506 context.

II. Covered Persons

We believe that the Commission should consider the implications of the very broad covered persons definition under proposed Rule 506(c). In our view, the final rule should be adjusted to better reflect the relative involvement of covered persons in a Rule 506 offering.

[1] See also the disclosures required by Items 401(f) and (g) of Regulation S-K.

A. Officers

1. The rule should be limited to executive officers of the issuer.

Under the proposed amendment to Rule 506, the disqualification provisions would apply to all "officers." We believe that limiting the scope of these provisions to "executive officers," as defined in Rule 501(f) of Regulation D[2], would be more appropriate, given their significantly greater influence on the policies of the issuer as compared to non-executive officers. We believe that applying the term "officer," as defined under Securities Act Rule 405, would result in an overly broad scope of disqualification. The term would include every "vice president" and also the company "secretary," persons who may not in fact have the power to influence or otherwise control the management of a covered entity. The title "vice president" is routinely granted to numerous persons within an organization (particularly in an investment bank serving as placement agent or initial purchaser), often with a further designation of a specific function, such as facilities, procurement, or other functions generally of little relevance to the conduct of the securities offering or overall executive management of the company. Because in virtually every situation non-executive officers report to executive officers, it is the latter who have policy-making authority.

By contrast, the term "executive officer," as defined in Rule 501(f) of Regulation D and Rule 3b-7 under the Securities Exchange Act of 1934, as amended (the "***Exchange Act***"), is well understood by issuers.[3] This understanding will foster compliance with the revised rule, and we believe that reference to this term would better achieve the legislative goal underlying Section 926, which is not to harm the ability of companies to engage in capital formation, but instead is intended to subject offerings in which a bad actor plays a significant role to greater regulatory scrutiny. Even within Regulation D, executive officers have special status and are considered "accredited investors" based on their participation in the policy-making functions of the issuer. To deviate from such a well-recognized system that differentiates the true key management of an issuer from its less important officers would require issuers to devote time and incur costs to make factual inquiries that, we believe, are unnecessary for the protection of investors. More importantly, the discovery that one or more of these non-executive officers are within the scope of persons whose employment would disqualify the issuer from relying on Rule 506 could have potentially disastrous consequences for the issuer. Therefore, we respectfully request that the Commission's final rule limit the covered persons subject to the disqualification provisions to the well-understood class of executive officers, rather than to the more subjective and overly broad group of officers.

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[2] Rule 501(f) defines "executive officer" to mean "the president, any vice president in charge of a principal business unit, division or function (such as sales, administration or finance), any other officer who performs a policy making function, or any other person who performs similar policy making functions for the issuer. Executive officers of subsidiaries may be deemed executive officers of the issuer if they perform such policy making functions for the issuer." See also the Commission's 2007 rule proposal in Release No. 33-8838 (August 3, 2007).

[3] The term "executive officers" focuses on persons who serve in policy-making functions and is used throughout the federal securities regulatory regime, including the comprehensive executive compensation disclosure requirements in Item 402 of Regulation S-K.

2. With respect to compensated solicitors, the rule should be limited to officers who are actually involved in the offering.

Section 926 is intended to exclude felons and other "bad actors" from participating in Rule 506 offerings, thereby protecting investors in those offerings. With respect to a compensated solicitor[4] that is not a natural person, we believe that the disqualification should be extended only to persons who actually participate in the offering. Particularly with respect to larger compensated solicitor firms that are organized by specialty areas or products, the inclusion of all general partners, directors, officers and managing members as covered persons simply casts too wide a net with no measurable benefit to investors. We recognize that the more fact-specific and detailed determination of who is actually involved in an offering may sometimes require the compensated solicitor firm to make judgments with respect to supervisory personnel. However, in most cases, we believe that this problem can be addressed by the firm specifically designating a management representative or representatives to monitor and oversee those persons actually involved in the offering. Because this would likely fall within the scope of the compliance function these firms would ordinarily be expected to perform, we do not believe this would impose an unreasonable burden on such firms, and the burden it does impose would be consistent with other compliance obligations such firms are mandated to perform.[5]

In the Proposing Release, the Commission noted the particular problems that could arise with respect to financial institutions that are acting as placement agents, since such entities typically have numerous "vice presidents," many of whom have no connection with the offering of securities. For this reason, if the Commission does not adopt our suggestion in Section II.A.1. above that the final rule should focus on executive officers rather than officers, we recommend at a minimum that the term "executive officer" should be substituted for the term "officer" with respect to compensated solicitors.

3. The Commission should provide for automatic waiver of disqualification for registered broker-dealers subject to disqualification based on state violations or orders.

Consistent with Section 926 and its mandate to the Commission to promulgate disqualification rules "substantially similar" to Rule 262, the Commission proposes to carry over the current waiver provisions of Rule 262 to the new disqualification provisions. Proposed Rule 506(c)(2)(i) provides that disqualification will not apply, "[u]pon a showing of good cause and without prejudice to any other action by the Commission, if the Commission determines that it is

[4] To avoid public confusion, we also recommend that the Commission explicitly address in the adopting release the necessity of broker-dealer registration, or associated person registration, for solicitors receiving transaction-based compensation. While it is possible for a person to act as an unregistered finder in connection with a securities offering, as a practical matter this would occur only under extremely rare circumstances.

[5] To assure that the enterprise itself is not within the "bad actor" category, we believe that the disqualification criteria may be appropriate if the chief executive officer or chief compliance officer of the firm falls within the category of bad actors.

not necessary under the circumstances that an exemption be denied." We endorse this aspect of the proposal.

The Commission has requested comment as to whether, and under what circumstances, it should exercise waiver authority under its disqualification rules for cases involving final orders of state regulators. We believe waivers should be available, and we further believe that the waiver should be automatic in circumstances where a broker-dealer or agent thereof subject to a disqualifying event based on a state violation or order continues to be a registered broker-dealer or agent in that state. If the sanctioning state has not concluded that the broker-dealer or agent should be denied the right to conduct business in that state, the Commission should defer to that determination. We see no reason why an issuer's offering should be delayed while the Commission undertakes a separate review, seeks concurrence by the relevant regulator or waits for lack of objection after notice. We also see no justification for the Commission to impose additional requirements beyond those that the state has imposed. To do so would negate the Congressional mandate for a unified federal and state exemption provided by the federal pre-emption of state regulation of Rule 506 offerings pursuant to Section 18 of the Securities Act.

If the Commission does not incorporate an automatic waiver in the final rule, we believe it should, at a minimum, provide an exception from disqualification if the relevant authority of the state to which the disqualification relates waives the disqualification. Paragraph (D)(2)(a) of NASAA's Model Accredited Investor Exemption (the "***MAIE***") includes such a provision, as does paragraph B.6 of NASAA's Uniform Limited Offering Exemption (the "***ULOE***"). By including a similar provision in Rule 506(c), the Commission would continue to respect the Congressional mandate for a unified federal and state exemption provided by the Rule 506 federal pre-emption provision.

B. 10% Beneficial Owners

We believe that the proposed inclusion of "any beneficial owner of 10% or more of any class of the issuer's equity securities" within the list of persons whose prior bad acts may disqualify an issuer from use of the Rule 506 exemption, in comparable fashion to the disqualification provision in Rule 262(b)(1) (applicable to both Regulation A offerings and those relying on Rule 505 of Regulation D), is unnecessary and, if included, should be substantially modified, for the reasons set forth below.

First, as applied to public companies seeking to rely on Rule 506, because neither Schedule 13D (specifically Item 2), Schedule 13G, nor Form 3 currently require 5% or 10% beneficial owners of a public company's securities who file such forms to report whether they may be deemed "bad actors" within the scope of any or all disqualifying events in the proposed rule, we believe it would be very difficult, if not impossible, for a public company to comply with the rule, unless such beneficial owners had a statutory or contractual obligation to provide the issuer with such information. A beneficial owner acquiring equity securities of a public company in the open market would generally have no obligation to disclose whether it is a "bad actor" within the scope of the proposed rule.

Second, many such beneficial owners may be solely passive investors with no ability or intent to control or otherwise influence the issuer's operations or its management unless that low level of ownership is in some manner coupled with other elements of control. We do not consider a 10% ownership interest to be significant enough to warrant disqualification of an issuer from use of the Rule 506 exemption, and that would be particularly the case if the class of equity securities owned by the person provides either no or limited voting rights.[6] Thus, if beneficial owners are to be considered at all among potential "bad actors," we suggest that the Commission adopt the presumptive control test from Section 2(a)(5) of the Investment Company Act of 1940, as amended (the "***Investment Company Act***"), whereby a person who beneficially owns more than 25% of the "voting securities" of a company is presumed to control that company. In turn, we believe that the Commission should incorporate the "voting securities" definition from Investment Company Act Section 2(a)(42), whereby the bad actor rule would apply only to those beneficial owners of equity securities of an issuer who are entitled to vote for the election of directors (or their equivalents) of the issuer.

Third, in the case of typical offerings under Rule 506 by hedge funds and other private investment funds, whereby the offered securities are sold on a continuing basis with quarterly, monthly or more frequent sales of new securities, and periodic redemptions by investors, a particular beneficial owner's interest in the issuer may constantly rise above or fall below the stated threshold, depending on sales and redemptions. While an issuer may obtain requisite representations in subscription agreements from new investors concerning whether they are "bad actors" at the time of investment, it would be virtually impossible to police investors whose interests are below the stated threshold one day, and above the threshold the next (to say nothing of depending on investors to immediately notify the issuer of any change in "bad actor" status). This "rolling test" results in several possible scenarios: (1) an issuer could refuse to accept a subscription from any prospective investor that represents that it is a "bad actor," regardless of the amount of voting securities covered by the subscription, so as to protect against the possibility that the subscriber's interest may exceed the threshold at some time in the future; (2) an issuer could prohibit investors from beneficially owning voting securities exceeding the threshold (or any voting securities) in case they may become "bad actors" at any time during their tenure as investors, enforcing that prohibition with a mandatory redemption or partial redemption of the investor's holdings in excess of the threshold; or (3) an issuer could create a separate class of non-voting securities for "bad actors," provided that such class may be offered and sold without integration with the issuer's voting securities being offered pursuant to Rule 506 (this scenario is somewhat analogous to what issuers that may invest in "new issues" within the meaning of FINRA Rule 5130 do in the case of investors who are "restricted persons" within the meaning of that Rule).

We note that by reason of the broad scope of the "bad actor" classification, an injunction or other penalty with respect to securities law violations by an investor in connection with a wholly unrelated matter would, under the proposed rule, disqualify an issuer in which the

[6] In this regard, we note that Rule 13d-1 under the Exchange Act defines the term "equity security" for purposes of filing Schedules 13D and 13G to exclude non-voting securities. This exclusion further exacerbates the difficulty in determining whether "bad actors" may be among the beneficial owners of a public company's securities.

investor is an over 10% owner from conducting a Rule 506 offering. Not only do we not see any means by which the issuer would be able to avoid this consequence under the proposed rule, we also believe that there exists the possibility that, unless the issuer actively monitors all litigation events affecting its larger security holders, the issuer may not even be aware of the issuance of the injunction or other penalty. If the Commission does not eliminate the disqualification by reason of a 10% holder's securities law violations, we encourage the Commission, in its final rules, to consider not applying the disqualification to violations that occur to the holder after the date of its investment bringing it over the 10% criterion (provided that at the date of the Rule 506 offering it does not own 50% of more of the issuer's securities).

C. Investment Advisers

While the Commission has not contemplated in the proposed rules that investment advisers and their directors, officers, general partners, and managing members would be considered "covered persons" for the purposes of the rule, we note that the Commission has solicited comment as to whether investment advisers and such associated persons should be included in the "covered persons" definition. We do not believe that investment advisers should be considered in the category of "covered persons" for purposes of the rule. In this regard, an investment adviser serves a markedly different function from the internal management of an issuer or fund, and is subject to fiduciary duties with respect to advisory clients. The role served by an investment adviser is unlikely to raise the concerns with respect to "bad actors" contemplated by the Dodd-Frank Act and proposed Rule 506(c). An issuer or fund client of an investment adviser will customarily have its own board of directors (or comparable management), including independent directors, who are in a better position to assess any legal or regulatory history that the investment adviser or its associated person may have, and who typically have authority to discharge the adviser for a variety of reasons (or no reason).

If the Commission were to decide to include investment advisers among the "covered persons" for the purposes of Rule 506(c), we believe that it would be appropriate to provide for an automatic waiver of disqualification with respect to any investment adviser that is registered with the Commission or a state securities regulator. Particularly following the changes to the rules governing registration of investment advisers promulgated pursuant to the Dodd-Frank Act, we believe that the Commission should recognize the fact that investment advisers will often be subject to the registration and attendant substantial regulation contemplated by the Investment Advisers Act of 1940, as amended (the "***Advisers Act***") and comparable provisions in state securities laws, such that any disqualifying event should be waived in recognition of the pre-existing comprehensive regulatory framework applicable to registered investment advisers. This could be an appropriate circumstance in which self-disclosure may be mandated, such as contained in Form ADV, Parts 2A and 2B, as noted above, if material to the offering. The prescribed disclosures could be contained in an offering-related document or, for efficiency, a copy of the investment adviser's Form ADV could be provided to prospective fund investors when the offer to purchase is made.

D. Affiliated Issuers

We do not believe that "affiliated issuers" should be included in the category of "covered persons" for the purposes of proposed Rule 506(c). The proposed rule refers to the issuer, any predecessor of the issuer or an affiliated issuer; however, the Commission's applicable rules (*i.e.*, Rule 501 of Regulation D, Securities Act Rule 405 and Regulation A) do not define the term "affiliated issuer" for the purposes of these rules. Applying the concepts associated with the definition of "affiliate" specified in Rule 405, an affiliated issuer would likely be considered any issuer that directly or indirectly, through one or more intermediaries, controls or is controlled by, or is under common control with, the subject issuer seeking to rely on Rule 506. Thus, for example, in the case of a large public company seeking to rely on Rule 506, it would be required to vet each of its distant majority-owned subsidiaries – even those that are not taking any part in, and are not receiving any proceeds from, the offering, to determine whether any of such entities is a "bad actor."

As an example in the private equity context, given the potentially broad reach of "affiliated issuer," it is possible that a private equity firm with a clean record could be disqualified from reliance on Rule 506 due to the bad acts of officers or directors at a portfolio company of which it owns only a small percentage. Similarly, a portfolio company seeking to rely on Rule 506 may be disqualified from so doing if it is under common control with a portfolio company that was disqualified as a bad actor, despite having a unique management and being engaged in different businesses. So long as the use of the offering's proceeds does not directly or indirectly inure to the benefit of the affiliated issuer that is subject to the statutory disqualification, it is unclear why a disqualifying event with respect to an affiliated issuer should disqualify the issuer of securities under Rule 506, rather than only serving as a disqualifying event with respect to the affiliated issuer if it were to seek to rely on Rule 506 itself. While this extension of Rule 506(c) may be appropriate in the context where both the issuer and the affiliated issuer are acting effectively as co-issuers with respect to the offering, such as when an affiliated issuer guarantees the securities of the issuer, we do not believe that any disqualifying events with regard to affiliated issuers outside of this context should serve to disqualify an issuer from its reliance on Rule 506.

Moreover, proposed Rule 506(c) contemplates a broad range of potential affiliates with a more direct bearing on the conduct of an issuer that could give rise to a disqualifying event, such as any director, officer, general partner or managing member of the issuer. The disqualification of an issuer arising from any "bad actors" among these categories of affiliates should address the concerns with respect to the conduct of the issuer's principal affiliates, such that it would not be necessary to extend the rule to cover disqualifying events of affiliated issuers that have no involvement in the particular offering.

If the Commission does determine to include "affiliated issuers" in Rule 506(c), we support the inclusion of proposed paragraph (c)(3) to Rule 506, which would exclude disqualifying events that occurred before the affiliation arose if the affiliated entity is not in control of the issuer or under common control with the issuer by a third party that was in control of the affiliated entity at the time of the otherwise disqualifying event. This, too, could be a

circumstance in which prescribed self-disclosure, to the extent material to the offering, may more effectively address the specific circumstances in a flexible manner.

E. Predecessor Issuers

While we recognize the importance of considering disqualifying events related to predecessors of an issuer, so that any interim transformative transactions would not serve to "cleanse" an issuer of disqualifying events, we are concerned that the term "predecessor issuer" may be over-inclusive when considering the availability of the exemption. For example, there may be situations where, as is contemplated in proposed paragraph (c)(3) of Rule 506 with respect to affiliated issuers, the predecessor issuer was controlled by a different group prior to the succession by the issuer, such that disqualifying events that occurred during that time should not be attributed to the successor issuer. For this reason, we suggest that the Commission consider adopting a similar approach as contemplated in paragraph (c)(3) with respect to predecessor issuers.

II. Disqualification Provisions

A. The Disqualification Provisions Specified in Paragraph (c)(1)(i) – Certain Convictions for Felonies and Misdemeanors.

The inclusion of a conviction of any felony or misdemeanor "in connection with the purchase or sale of any security" in subparagraph (A) or arising out of the conduct of a business of an underwriter pursuant to subparagraph (C) potentially cover criminal convictions for technical violations of statutory provisions or rules, in certain instances without any need for the prosecutor to prove scienter, particularly in the case of state securities laws. For example, there is no fraudulent intent required for a conviction under Section 359-g.2 of Article 23-A of the New York General Business Law (the "***NYGBL***," New York's "Blue Sky" law, popularly known as the "Martin Act"):

> "Any person, partnership, corporation, company, trust or association violating any of the provisions of this article shall be guilty of a misdemeanor, except where otherwise provided herein, punishable by a fine of not more than five hundred dollars, or imprisonment for not more than one year or both."

By reason of that provision, an issuer criminally charged by the New York Attorney General's office with a litany of counts alleging fraud in connection with a prior securities offering in violation of NYGBL Section 352-c (New York's adjunct to Section 10(b) of the Exchange Act),[7] as well as counts for failing to make certain filings in violation of NYGBL Section 359-e, but ultimately convicted only of a misdemeanor count of failing to file an innocuous "further state notice" form, as required by NYGBL Section 359-e.8, could be barred under the proposed rule as a "bad actor," absent a waiver by the Commission.

[7] Certain intentional violations of Section 352-c may be prosecuted as felonies, rather than misdemeanors.

Further, an issuer could be barred as a "bad actor" as a result of a state criminal conviction arising out of a failure to file a Form D, or for a failure to make a timely filing of such form, in connection with a prior Rule 506 offering, in violation of its Blue Sky law. For example, an issuer could be prosecuted under Section 11-705(1) of the Maryland Securities Act (the "***MSA***") for failing to make a Form D filing or making a late Form D filing in violation of MSA Section 11-503.1(d) and Rule 02.02.09.09 thereunder. Under Section 11-705(1), a person who willfully violates Section 11-503.1 or a rule thereunder "is subject to a fine not exceeding $50,000 or imprisonment not exceeding 3 years or both" (which presumably qualifies as a felony).[8]

While we recognize that criminal prosecutions for securities law violations are typically restricted to cases involving serious financial crimes, there are many instances where a state or federal prosecutor may initially "overcharge" a defendant with committing numerous violations of law, but where the case is eventually resolved with either a verdict or negotiated plea in which the defendant is convicted solely of some technical violation of law far less severe than the crimes initially charged. We believe that felonies and misdemeanors within the scope of the proposed rule should be restricted to those involving serious crimes, such as fraud or larceny, and in which proof of *scienter* is a necessary element.

With regard to the Commission's request for comments on this paragraph, we believe that the proposed five-year and ten-year look-back periods for issuers and other covered persons premised on criminal convictions are appropriate. There is no indication in Section 926 that Congress intended to impose different look-back periods, the sole reference being the incorporation of Rule 262. Unless a criminal conviction also entailed some form of permanent bar from the securities business, we see no basis for extending the period of disqualification.

Further, we believe that an entity that has undergone a change in control since the time of a criminal conviction, or a criminal conviction of an issuer's current affiliate at a time when the parties were not affiliates, should not result in a disqualification, as set forth in paragraph (c)(3). A presumption of control based on holding over 25% of voting securities would be appropriate, as discussed above. We believe that the criminal convictions listed are too broad, and as such we believe that such criminal convictions need not be expanded to cover other types of crimes not mandated by the Dodd-Frank Act. Further, given that criminal prosecutions in foreign courts may not provide the same due process rights that apply to criminal proceedings in the United States, we believe it is clearly inappropriate to expand the rule to encompass any such foreign convictions. Nonetheless, because information about foreign court proceedings and related

[8] It is noted that the failure to file a Form D is not a condition of Rule 506, as confirmed by: (i) Questions 257.07 and 257.08 of the Compliance and Disclosure Interpretations of the SEC's Division of Corporation Finance, available at http://www.sec.gov/divisions/corpfin/guidance/securitiesactrules-interps.htm ; and (ii) several court decisions, including In re Ressler Hardwoods and Flooring, Inc., 2009 Bankr. LEXIS 4441 (Bankr. M.D. Pa. 2009), in which the court construed a Rule 506 offering to a Maryland investor and concluded that the issuer's failure to file any Form D for its Rule 506 offering under the MSA did not affect its claim of "covered security" status under Section 18 of the Securities Act or give rise to a claim for rescission or damages under MSA Section 11-703 for a sale of unregistered securities in violation of MSA Section 11-501.

records may be difficult for a U.S. investor to identify or obtain, self-disclosure of foreign criminal convictions, to the extent material to the offering, may allow each prospective investor to identify and assess its relevance to the investment decision.

B. The Disqualification Provisions Specified in Paragraph (c)(1)(ii) – Certain Orders, Judgments and Decrees of any Court of Competent Jurisdiction.

We note that an "order, judgment or decree of any court of competent jurisdiction" may entail a temporary injunction or restraining order issued on an *ex parte* basis, without prior notice to the defendant, although the defendant will typically be given notice after the injunction or order is issued so that it may be challenged. In many instances, however, a defendant may decide not to challenge such an injunction or order, and will allow it to be converted into a permanent injunction, typically if counsel believes success on appeal is unlikely and the challenge would be extremely costly, and especially if the order is premised on an alleged violation of an innocuous provision of securities law.

Again, as is the case for disqualifications premised on criminal convictions, disqualifications arising out of civil actions within the scope of this provision may be premised on a purely technical violation of a securities law, rule or order. For example, the Maryland Securities Commissioner may bring a civil action under MSA Section 11-702, alleging that a person is about to engage in, or has engaged in, "a violation of any provision of this title or any rule or order under this title," and seek a temporary restraining order or temporary or permanent injunction (in the case of persons who allegedly already violated the MSA, the Commissioner may also seek a civil penalty up to $5,000 per violation, a declaratory judgment, appointment of a receiver or conservator, an asset freeze, rescission, restitution, and "any other relief the court deems just"). Thus, in lieu of a criminal prosecution of an issuer for failure to file, or a late filing of, a Form D for a prior Rule 506 offering, the Commissioner may seek injunctive relief against the issuer for the same violation, and obtain the same disqualifying result, absent the grant of a waiver by the Commission.

We believe that no court order, judgment or decree should be considered as the basis for disqualification unless it has been issued in a proceeding in which the defendant has been given prior notice and an opportunity to appear, and that all appeals have been exhausted or the time to appeal has expired. Furthermore, we believe that any such order, judgment or decree should be premised on violations of anti-fraud provisions or, at the very least, a failure to register securities offering or as a broker-dealer, agent, investment adviser, or investment adviser representative, and not on the basis of some technical filing or post-registration requirement or some other technical requirement of applicable securities law.

We also note that many securities law civil or criminal enforcement actions are resolved by the entry of an injunction enjoining a party from future violations of the securities laws, without assessing any monetary or other penalty against the party. In those instances where a party is only required to do (or refrain from doing) in the future that which it is already legally obligated to do (or refrain from doing), we believe that a reasonable basis exists for not extending the scope of the Rule 506 disqualification provisions to such a party. First, the

absence of a monetary sanction or other penalty suggests that the prior violation of law may have only been inadvertent or technical, without any adverse consequence to investors or others.[9] Alternatively, it may mean that the basis upon which the claim was brought was inadequate or weak, and both the government and the party charged determined that resolving the matter by means of such an injunction would be in the best interests of both parties. We believe that resolution of enforcement actions by means of such injunctions serve important public policy purposes, and that the imposition of a disqualification based on such injunctions would decrease the likelihood that some parties would consent to, or acquiesce in, the entry of such judgments. Moreover, we believe a Rule 506 disqualification based on such non-punitive injunctions may be wholly out of proportion to the securities law offense alleged in the underlying action. We believe it is one thing to limit the disqualification to "felons" and other bad actors, but we consider it something else to impose the same drastic consequences on persons whose only securities law violations may have been technical. We therefore suggest that in its final rules the Commission provide that the Rule 506 disqualification not apply to a party that is enjoined from future violations of the securities laws, without the assessment of any monetary or other penalty against the party. We suggest that the Commission consider proposing a similar rule amendment to Rule 262.

Further, we believe that in its final rule, the Commission should limit the scope of disqualification to persons specifically named in an order, and not all those who may be within a much larger class of persons brought within the scope of an order. For example, in a court order entered in a recent action brought by the Commission against J.P. Morgan Securities LLC, the court's injunction applied not only to the named defendant, but also to all of its "agents, servants, employees, attorneys, and all persons in active concert or participation with them who receive actual notice of this Final Judgment by personal service or otherwise."[10] Although the named defendant in an action may be subject to disqualification, it would, in our view, be completely inappropriate to extend the taint of the disqualification to the hundreds, and perhaps thousands, of the defendant's agents, servants, employees, attorneys and others acting in concert with them. If the Commission does not agree to adopt an exclusion from the scope of the disqualification for court orders limited to injunctions from future violations, we encourage the Commission, in its final rule, to make clear that the scope of the disqualification applies only to those defendants specifically named in an action.

With regard to the Commission's request for comments on this paragraph, we see no reason to impose look-back periods longer than those imposed under Rule 262. Moreover, we believe that a five-year look-back period should be applied consistently to all orders and injunctions within the scope of this provision. We believe that there is no reason to extend the

[9] An example of such a violation may include, for example, an investor who inadvertently failed to timely file a Schedule 13D or 13G.

[10] See SEC v. J.P. Morgan Securities LLC, C.A. No. 11-3877-WJM (D. NJ. July 8, 2011), *available at* http://sec.gov/litigation/litreleases/2011/lr22031-judgment.pdf . We note that in this action the defendant was ordered to pay monetary penalties in addition to being subject to injunctive relief. We therefore cite this case only as a recent example of the scope of injunctive relief that the Commission requested and the court ordered, which may extend significantly beyond the named defendant.

disqualifying period; certain injunctions or orders may be "permanent" only in the sense that they bar the defendant from engaging in any act or practice in violation of a securities law that the defendant is obligated to comply with anyway. The five-year look-back allows consideration of more current activities by the covered persons. Given that the regulatory orders in paragraph (c)(1)(iii) are issued in an administrative law context, rather than in a judicial context, we believe that court orders and injunctions should be treated in a different manner. Further, as is the case with foreign criminal prosecutions, in the absence of any assurance that foreign courts provide any due process to defendants in civil injunctive proceedings in the same manner provided in U.S. courts, there is no reason to disqualify issuers based on foreign civil proceedings.

C. The Disqualification Provisions Specified in Paragraph (c)(1)(iii)(A) – Certain Orders Under Administrative Proceedings

In response to the Commission's request for comment, we believe that the rules should clarify what is meant by a "bar," and we agree with the Commission that the absence of the word "bar" in an order should not be crucial to the determination of whether a disqualifying event has occurred. While it is not clearly mandated by Section 926, we believe that it would be reasonable for the Commission to provide a cut-off date in this provision, even if the particular order appears to provide a permanent bar and has no proviso for re-application. The term "final order" should be defined so as to be restricted to orders issued only after the defendant has been given notice and an opportunity to be heard, and has either exhausted any appeals or the time to appeal has expired. While the FINRA definition is helpful, we believe that it should also encompass the due process considerations discussed above. We support the addition of the specified language from Section 604 of the Uniform Securities Act (2002) to proposed Rule 506(c).We believe that a reference to an order being deemed "final" in accordance with any applicable law would also be helpful; however, it would not be problematic if a particular law does not specifically address whether and when an order would be deemed "final." While we recognize that the Commission should be the ultimate arbiter of what orders are deemed "final" within the scope of this provision, we believe that the rule could provide a mechanism for seeking the views of the particular regulator for an advisory, but non-binding opinion.

D. The Disqualification Provisions Specified in Paragraph (c)(1)(iii)(B) – Final Orders Based on "Fraudulent, Manipulative or Deceptive" Conduct

We note that the inclusion of a final order "based on a violation of any law or regulation that prohibits fraudulent, manipulative, or deceptive conduct" may encompass conduct that is not truly "fraudulent, manipulative or deceptive," but only defined as such in the particular statute. For example, under Advisers Act Rule 206(4)-6, Proxy Voting, it is a "fraudulent, deceptive or manipulative act, practice or course of business" within the meaning of Section 206(4) of the Advisers Act for an investment adviser to exercise voting authority with respect to client securities unless the adviser adopts and implements specified written policies and procedures pertaining to proxy voting. Characterizing the failure to have such policies as "fraudulent, deceptive or manipulative" has more to do with statutory authority under which the rule was adopted than the true nature of the offense.

Further, at the state level, NYGBL Section 352.1 provides that violations of any provision of NYGBL Art. 23-A "are hereby declared to be and are hereinafter referred to as a fraudulent practice or fraudulent practices." Accordingly, while the New York Attorney General has no current statutory authority to issue an administrative order within the scope of paragraph (c)(1)(iii)(B) for a violation of NYGBL Art. 23-A, if such authority were ever granted, or if another state's securities law, where the administrator has authority to issue such orders, designated any violation of the law or any rule or order thereunder to be "fraudulent, manipulative, or deceptive," many issuers could be disqualified from using Rule 506, premised solely on an unintentional technical violation of the law or a rule or order. The rule should specify the types of conduct involved, and not leave it up to a state's defining (or redefining) any and all violations of law to be "fraudulent, manipulative, or deceptive," so as to cause a disqualification.

Further, we believe that a common law standard would be appropriate, as would inclusion of a *scienter* standard. While we recognize that the Commission should be the ultimate arbiter of whether particular conduct is within the scope of this provision, we believe that the rule could provide a mechanism for seeking the views of the particular regulator for an advisory, but non-binding, opinion.

E. Orders of the CFTC or Other Regulators

The Commission is soliciting comment on whether final orders of the U.S. Commodity Futures Trading Commission (the "***CFTC***") or other regulators should serve as disqualifying events for the purposes of proposed Rule 506(c). We do not believe that the language of Section 926 establishes any basis upon which to extend the disqualification events to those involving parties other than the SEC, state regulatory authorities, and banking and insurance regulators. We are not aware of any evidence to suggest that the conduct that could be subject to an order from the CFTC should serve as a disqualifying event for federal securities law purposes under proposed Rule 506(c), and likewise we are aware of no basis to conclude that regulatory orders from entities outside of those entities specified in Section 926 and under Regulation A would present reasons to establish disqualifying events under Regulation D.

Nonetheless, Section 753 of the Dodd-Frank Act amended Section 6(c) of the Commodity Exchange Act to prohibit manipulation and fraud in connection with any swap, or a contract of sale of any commodity in interstate commerce, or for future delivery on or subject to the rules of any registered entity. Conduct violating these prohibitions would be highly relevant to prospective investors. While lacking a Congressional mandate to predicate disqualification upon the CFTC's orders, this may be an appropriate subject for the Commission to address through prescribed self-disclosures, to the extent material to the offering.

F. Orders from Jurisdictions Outside of the United States

As noted above, we do not believe that the disqualifying events contemplated in Rule 506(c) should extend beyond the borders of the United States. Nothing in Section 926 specifically discusses disqualifications arising from proceedings occurring in foreign

jurisdictions, such as foreign criminal convictions, foreign civil court orders, orders arising from foreign regulatory proceedings or other similar events. Rather, we believe that it is clear from Section 926 that the contemplated disqualification events are limited to U.S. federal and state law. Similarly, Rule 262 does not currently contemplate any consideration of actions taken in foreign jurisdictions for the purpose of establishing disqualification events under Regulation A, and we do not believe that the implementation of Section 926 requires any such expansion. Although some foreign jurisdictions afford defendants a presumption of innocence and procedural safeguards, this is not the case uniformly. An issuer's disqualification from use of Rule 506 by reason of proceedings in a foreign jurisdiction that did not provide the person charged comparable procedural and jurisprudential standards to those in the United States would be offensive to traditional notions of fair play and substantial justice.
Also, as the Commission is aware, for public policy reasons not all foreign judgments are entitled to enforcement in the United States. The imposition of a *per se* disqualification based on foreign proceedings would therefore also be offensive to public policy.

We believe that the addition of any disqualification events tied to the laws of foreign jurisdictions would significantly expand the scope of Rule 506(c) and thereby significantly increase the burdens on issuers seeking to rely on Rule 506 to conduct a private placement – without, we submit, any concomitantly greater protection of U.S. investors. As it has done with Regulation S, the Commission should continue to recognize the limitations of its extraterritorial power to enforce the registration provisions of Section 5 of the Securities Act (as contrasted with its antifraud authority). For these reasons, we believe that it may be appropriate for the Commission to specify expressly in Rule 506(c) that the new disqualification provisions do not extend to any court, regulatory or exchange convictions, orders, judgments or other actions arising in jurisdictions outside of the United States

G. The Scope of Disqualification Events

In sum, we believe that the final rules should specify that a determination of *scienter* is required in order for specified conduct deemed violative of applicable state or federal laws, rules or regulations to be considered a disqualification event. Absent the requisite intent to defraud, we do not believe that it is appropriate that, for example, actions involving faulty disclosures or filings or other technical violations should serve as a basis for establishing a disqualification event.

III. The "Reasonable Care" Exception

We commend the Commission for proposing a "reasonable care" exception from the proposed disqualification provisions, and share the Commission's "concern that the benefits of Rule 506—which, among other things, is intended to create a cost-effective method of raising capital, particularly for small businesses—may otherwise be substantially reduced."[11] Moreover,

[11] Proposing Release at pp. 41-42 (emphasis added).

we agree that a proper balance must be struck between the drastic consequences of the Securities Act Section 5 or state Blue Sky law securities registration violation attendant to the heightened risk of loss of safe-harbor coverage,[12] on the one hand and, on the other hand, issuers' "responsibility to screen bad actors out of their Rule 506 offerings." However, we believe that the vague parameters of the proposed exception, coupled with the breadth of the "covered person" definition and draconian retroactivity feature that have been proposed, will deter many issuers, including (but not limited to) the smaller issuers whose ability to raise capital has again become a focal point for possible regulatory reform,[13] from utilizing Rule 506. This prospect, in the worst case, could foreclose access by smaller issuers to lower-cost capital by forcing them to resort to a "traditional" private placement based on the relatively sparse and sometimes inconsistent case law defining Section 4(2).[14] Exclusive reliance upon the statutory private placement exemption not only would increase significantly the risk of a Section 5 violation, but also would deny issuers the benefits of pre-emption of state securities law registration requirements provided by Section 18 of the Securities Act, thereby exposing them to the substantially greater costs and risks of compliance with, and/or violation of, a myriad of state blue sky laws.

While we recognize and appreciate the Commission's traditional aversion to "bright-line" tests for reliance upon a non-exclusive Section 5 safe harbor, for fear of generating a roadmap for possible evasion, we nevertheless urge the Commission to facilitate issuer compliance by outlining clearly, either in the rule itself or in the adopting release, more specific guidelines for the exercise of "reasonable care." In this regard, we do not disagree with the Commission's determination to impose on issuers the burden of establishing that "reasonable care" has been exercised in connection with a particular offering. By the same token, we do believe strongly that it is neither appropriate nor fair to leave the definition of what conduct will (or, perhaps more importantly, will not) satisfy the requisite standard of care in the litigation process.[15] That said, we would like to offer a few suggestions for clarification that we think would enhance the utility of the proposed exception, yet still redound to the benefit of investors in private placements structured to comply with the terms and conditions of Rule 506.

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[12] As if to underscore this risk, the Commission expressed its belief (in footnote 83 of the Proposing Release) that the curative benefits of Rule 508 – providing that "insignificant deviations' from the terms, conditions and requirements of Regulation D will not necessarily result in loss of the exemption from Securities Act registration requirements" – would not be available in "circumstances in which an offering was disqualified based on Proposed Rule 506(c)."

[13] *See, e.g.*, Testimony of Commission Chairman Mary L. Schapiro, *On the Future of Capital Formation*, Before the U.S. House of Representatives Committee on Oversight and Government Reform (May 10, 2011), *available at* http://www.sec.gov/news/testimony/2011/ts051011mls.htm; Letter From Commission Chairman Mary L. Schapiro to the Hon. Darrell E. Issa, Chairman, Committee on Oversight and Government Reform, dated April 6, 2011.

[14] For a discussion and analysis of the relevant jurisprudence, see Committee on Federal Regulation of Securities, American Bar Association Section of Business Law, *Law of Private Placements (Non-Public Offerings) Not Entitled to Benefits of Safe Harbor – A Report*, 66 Bus. Law. 85 (Nov. 2010).

[15] According to the Commission, "the burden would be on the issuer to establish that it had exercised reasonable care (most likely in the context of an enforcement proceeding brought by a regulator or a private action brought by investors)." Proposing Release at 41.

It is important that the Commission clarify its expectations regarding the required "factual inquiry" for both issuers and market professionals engaged in the solicitation process. With respect to issuers, we suggest that the Commission amplify its statement (at p. 42 of the Proposing Release) that issuers may be entitled "in some circumstances" to rely on questionnaires to directors, officers and significant shareholders, and other, unidentified "screening and compliance mechanisms" in conducting the necessary diligence on their affiliated "covered persons." Examples of what the Commission might consider to be "reasonable" for, respectively, pre-IPO private companies, smaller reporting companies, and larger public companies, would be very helpful. We further recommend that the Commission affirmatively state – either in the text of the final rule amendment or in the adopting release – that an issuer may properly rely on written representations or certifications from placement agents, finders and any other person or entity (whether or not regulated) hired by or on behalf of the issuer to solicit in connection with an offering, relating to the "bad actor" status of their respective "covered persons," absent facts putting the issuer on notice that such certifications or representations are materially false, misleading or otherwise unreliable.[16] Moreover, issuers should be permitted to take any other measures to conduct diligence on their own personnel as well as third-party covered persons. In its adopting release, we request that the Commission recognize that what constitutes a reasonable factual inquiry may vary from issuer to issuer, based on a number of factors, including the size and organizational structure of the issuer, and the resources available to the issuer.

As to market professionals, we again believe that the Commission should develop (or direct FINRA to develop) concrete standards for inquiry that would be applicable at a minimum to those persons or entities subject to Commission or state regulation (*e.g.*, registered broker-dealers and investment advisers). As one commenter pointed out, the Commission has taken a similar approach in the Rule 144A context without any apparent adverse consequences to investors in unregistered offerings.[17] It is noted that in the case of a large broker-dealer acting as placement agent, it may be impossible, or nearly impossible, for an issuer to vet all registered representatives who may offer and sell the issuer's securities, unless the placement agent were to agree to restrict such representatives to specific persons who go through a pre-screening process; this can be a cumbersome and time-consuming exercise. In lieu of the issuer assuming this responsibility, we believe that a representation, warranty and covenant by the placement agent to use only non-disqualified personnel to offer and sell the securities should suffice.

Finally, as discussed in Section II of this letter, the Commission also would facilitate compliance in this area by narrowing the universe of relevant "covered persons." To be

[16] *See, e.g.*, FINRA Rule 5130, permitting reliance on written representations for up to 12 months, with "no change" updating via negative consent letters to be furnished annually thereafter. At least one other commenter has recommended such an approach to the Commission. *See* Letter from Sullivan & Cromwell, dated July 14, 2011, *available at* http://www.sec.gov/comments/s7-21-11/s72111.shtml .

[17] Letter from Cleary, Gottlieb Steen & Hamilton, dated July 14, 2011 (citing the example of seller reliance on QIB eligibility certifications set forth in the Rule 144A adopting release), *available at* http://www.sec.gov/comments/s7-21-11/s72111.shtml .

workable, at least as applied to market professionals retained by the issuer to solicit potential investors, this definition should focus on individuals actually participating in the specific Rule 506 offering (assuming the entity that employs them is not itself disqualified).

IV. Waivers

A. The Waiver Process – Delegation of Authority

We believe that it is critical to the proper functioning of the proposed disqualification provisions to have an effective and efficient waiver process. In this regard, we support the Commission's proposal to carry over the Commission's waiver authority currently contemplated in Regulation A to proposed Rule 506(c).

However, we believe that it is critical for the Commission to adopt an approach consistent with Regulation A whereby the Commission delegates authority to grant waivers to the Director of the Division of Corporation Finance. We are not aware of any concerns expressed by the Commission or others with regard to the ability of the Division of Corporation Finance to grant waivers in the context of Regulation A or for other similar purposes. In fact, we believe that the current approach of delegating the consideration of waiver requests to the Director of the Division of Corporation Finance and then further sub-delegating to the Office of Small Business Policy in the Division of Corporation Finance provides the best mechanism for the timely consideration of waiver requests in a consistent manner. The Commission has not articulated any reason why the consideration of waivers under Rule 506(c) should instead be conducted by obtaining a direct order of the Commission, and there otherwise appears to be no reason why the process should be handled differently as compared to the waiver of the applicability of other rules administered by the Division of Corporation Finance. Given these factors, we believe the best approach would be to delegate authority for the consideration of waivers to the Division of Corporation Finance.

B. Guidelines for Waivers

We do believe that it would be useful for the Commission to establish, whether by rule, by Commission interpretation or by staff statement, guidelines specifying the circumstances that are likely to give rise to the grant or denial of a waiver. We note that the staff of the Division of Corporation Finance has recently provided such helpful guidance in the context of waivers from the status as an "ineligible issuer" for the purpose of satisfying the requirements under the definition of "well-known seasoned issuer."[18] The Commission and the Staff of the Division of Corporation Finance have had a significant amount of experience considering waiver requests with respect to Rules 262 and 505,[19] and therefore there should be a sufficient basis upon which to establish parameters under which waivers would be granted (recognizing that the outcome of

[18] SEC Division of Corporation Finance Statement on Well-Known Seasoned Issuer Waivers (July 8, 2011), available at http://sec.gov/divisions/corpfin/cfguidance.shtml#wksi-waivers

[19] SEC Division of Corporation Finance no-action letters pertaining to Section 3(b) of the Securities Act, *available at* http://www.sec.gov/divisions/corpfin/cf-noaction.shtml#3b .

each individual request will turn on its own facts and circumstances). These sorts of guidelines would put each requestor on notice of situations when a waiver is not likely to be forthcoming, and therefore could serve to discourage meritless and futile waiver requests.

C. Automatic Waivers Based on State Action

We believe that it is appropriate for the Commission to include a provision, as is currently included in the MAIE and ULOE, that would serve to automatically provide an exception from disqualification in situations where the relevant authority of the state to which the disqualification relates waives the disqualification. In this regard, we believe that the Commission should show sufficient deference to the determinations of the state regulators so that the Commission will not be placed in a position of "second guessing" the determinations of such regulators.

By contrast, where the state regulators have not acted to waive a disqualification, we believe that it is appropriate for the Commission to consider waiver requests with regard to final orders of state regulatory authorities to determine if a waiver of such disqualification provision is warranted. We do not think that any formal process for the Commission's consultation with the relevant state authorities is necessary in these cases because the Commission is determining compliance with respect to its own rules, rather than compliance with the underlying final order of the state authority.

VI. Transition Issues

The Commission has indicated that proposed Rule 506(c) will be implemented in a manner such that past disqualification events would be considered for the purposes of the rule. The Commission has not proposed to address, in the form of any exemption, grandfathering provision or otherwise, the status of potential disqualification events that occurred prior to the enactment of the Dodd-Frank Act and the effective date of the proposed amendments to Rule 506. The Commission notes that the statutory and the legislative history of Section 926 lead it to this result; however, we note that Section 926 does not specifically mandate or otherwise refer to the possibility that its provisions should apply retroactively upon adoption of implementing rules by the Commission.

A. Impact of the Retroactive Application of Proposed Rule 506(c)

We are concerned that the retroactive application of the disqualification provision specified in proposed Rule 506(c) would unduly harm parties who resolved prior actions without fair notice of the potential implications the resolution might have on the parties' ability to conduct or participate in future Rule 506 offerings. It is entirely possible that a potential covered person may have negotiated a different outcome in a regulatory or other action if the draconian consequence of proposed Rule 506(c) were known or contemplated at the time of such action. This result, in our view, would unfairly penalize issuers seeking to conduct private offerings under Rule 506 and could thus significantly impair their ability to raise capital in the most efficient manner.

We agree with the remarks of Commissioner Paredes that not only is retroactive application a bad policy decision, it is contrary to the Supreme Court's application of *Landgraf* and other court decisions concerning other new Commission enforcement remedies.[20]

B. Commission Precedent for Handling Disqualification Provision Prospectively

We believe Commission action to apply the disqualification provisions prospectively only (at least from the time of the enactment of the Dodd-Frank Act, but preferably from the effective date of the final rules) would be entirely consistent with how the Commission has approached analogous bad actor disqualification provisions in the past, notably the "ineligible issuer" provisions of the Securities Offering Reform rule changes adopted in 2005, and before that the disqualification provisions contained in each of the statutory safe harbors for forward-looking statements in Section 27A of the Securities Act and Section 21E of the Exchange Act pursuant to the Private Securities Litigation Reform Act of 1995. We see no reason why the Commission, even in light of the language of the Dodd-Frank Act that it cites in the Proposing Release, could not take the same approach today and not apply the disqualification provisions of proposed Rule 506(c) on a retroactive basis.

C. Grandfathering and Waiver Approaches in the Event of Retroactive Application

In the event that the Commission ultimately determines to adopt proposed Rule 506(c) in a manner where past disqualification events would be considered for the purposes of the rule, we do believe that the Commission should consider adopting a "grandfather" provision that would specifically apply with respect to those disqualification events that resulted from any settled civil proceeding arising prior to the effective date of the amendment to Rule 506(c), in tandem with the automatic recognition for Rule 506(c) purposes of previously granted waivers of comparable disqualification provisions under Rule 262 and Rule 505 of Regulation D. In addition, or alternatively if the Commission elects to not adopt a grandfathering approach of the type discussed here, the Commission (through its Division of Corporation Finance, acting via delegated authority as discussed above) should stand ready to consider waiver requests under Rule 506(c) that specifically relate to the potential harm imposed as a result of the retroactive application of the rule.

D. Treatment of Ongoing Offerings

We do not believe that the Commission's interpretation of the statute to require retroactive application to past disqualification events should serve to render ongoing or continuous offerings no longer eligible to rely on the Rule 506 exemption. In this regard, we suggest that the Commission specifically address in proposed Rule 506(c) that an offering commenced prior to the effective date of the final rules will not be disqualified by the presence

[20] SEC Commissioner Troy A. Paredes, Speech at Open Meeting for Proposed Rules Regarding Disqualification of Felons and Other Bad Actors from Rule 506 Offerings (May 25, 2011), available at: http://www.sec.gov/news/speech/2011/spch052511tap-item1.htm .

of a disqualifying event that occurred in the time period prior to the effective date of the final rules.

E. Transition

We suggest that the Commission adopt a phase-in period of at least six months for the effective date of Rule 506(c). A delayed effective date will allow issuers to establish procedures and conduct the necessary due diligence to determine whether disqualification events exist and must be considered, implement the procedures contemplated for the purposes of establishing the reasonable care exception, and taking all of the other steps necessary to ensure that offerings under Rule 506 can proceed in light of the significant changes to the eligibility standards for the rule. We believe that it would be unreasonable and inconsistent with the Commission's efforts to facilitate capital formation to impose a very short transition time following adoption of the final rules.

VII. Uniformity

We believe that the disqualification provisions in the Commission's exempt offering rules that have such provisions should be uniform. The existing provisions in Regulation A, Rule 505 of Regulation D and Rule 602 of Regulation E under the Securities Act are substantially similar to the proposed provisions in Rule 506, but they are different in ways that can result in higher compliance costs. As the Commission mentioned earlier in the proposal, Rule 262, for example, is drafted in a confusing two-tier framework. Issuers attempting to comply with the rule could benefit significantly from a more straightforward approach.

In addition, the disqualification provisions now in place have raised numerous interpretive issues and are overly broad. These problems of interpretation would be exacerbated if the Commission were now to adopt a separate provision for Rule 506 offerings that is similar but not exactly the same. We believe the Commission should take this opportunity to adopt one set of clear and updated disqualification provisions applicable to all the relevant exemptions. Although interpretive questions may arise, if the disqualification provisions are the same across different exemptions, the staff and the Commission will be better able to provide efficient and consistent guidance that can have a helpful impact on more offerings. Moreover, given the Commission's interest in investor protection, it is not clear why there should be any difference in the disqualification provisions across these exemptions.

We agree with the Commission's concern that, to the extent the provisions are different, it could encourage "bad actors" to concentrate on particular types of exempt offerings in ways that would taint the market for whichever types of offerings have the least restrictive provisions.

To the extent that the Commission does conform the disqualification provisions across all the relevant exemptions, we believe that it is imperative that the Commission provide a "grandfathering" provision of at least six months for any on-going offering under the existing exemptions. Certainly under Rule 504 the disqualification provisions would be new and a disqualification in the middle of an offering, particularly given the precarious state of the

financial markets for smaller companies, could prove devastating. Issuers and their covered persons may need to make adjustments to their management structure. Issuers may need to contract with different placement agents. Placement agents may need to assign different associated persons to handle or supervise the offering. In addition, although in theory the new provisions will be substantially similar to the existing rules for other exemptions, there could be unintended or small differences that could impact participation in an ongoing offering. Given that that type of difference may not be immediately obvious, it is very important that the Commission's action to encourage uniformity and to reduce cost and confusion not have a destructive effect on an on-going offering.

VII. Conclusion

We appreciate the opportunity to comment on the Commission's proposed amendments under Section 926. We hope that in implementing this important investor protection provision, the Commission carefully weighs the potential burden on capital-raising, particularly by smaller issuers that frequently rely on private placements under Rule 506 of Regulation D.

_/s/ Jeffrey W. Rubin_____
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Chair of the Federal Regulation of Securities Committee

_/s/ Shane B. Hansen_____
Shane B. Hansen
Chair of the State Regulation of Securities Committee

_/s/ Gregory C. Yadley_____
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