

SEC Amends Private Placement Rules to Remove the Ban on General Solicitation

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On July 10, 2013, the SEC adopted rules that eliminate the longstanding prohibition against the use of general solicitation and general advertising in private offerings made in reliance on Rule 506 of Regulation D under the Securities Act. These rules become effective on September 23, 2013. The SEC also issued for public comment proposed rules that are intended to enhance the SEC's understanding of market practices in Rule 506 offerings and to address investor concerns related to the removal of the prohibition against general solicitation in Rule 506.

The final rules amend the safe harbor from Securities Act registration provided by Rule 506 to remove the prohibition against general solicitation and general advertising. The final rules add a new subsection (c) to Rule 506 that permits the issuer (and any selling agents) to use general solicitation to offer and sell securities under Rule 506, so long as the following conditions are satisfied:

- the issuer must take reasonable steps to verify that the purchasers of the securities are accredited investors using a principles-based method of verification;
- all purchasers must be accredited investors at the time of the sale of the securities because they come within any of eight enumerated categories in Rule 501(a), or the issuer reasonably believes they come within one of those categories; and
- all terms and conditions of existing Rules 501 (definitions), 502(a) (integration restriction) and 502(d) (resale limitations) of Regulation D must be satisfied.

Prior to the amendments, an offering or sale of securities was only eligible for the Rule 506 safe harbor if there had been no general solicitation or general advertising in connection with the offer or sale.

The final rule includes a non-exclusive list of methods that issuers may use to satisfy the requirement that it take reasonable steps to verify that purchasers are accredited investors, including

- reviewing copies of any IRS form that reports the income of the purchaser for the two most recent years and obtaining a written representation from the purchaser that he or she has a reasonable expectation of reaching the necessary income level in the current year;

- reviewing documentation dated within the prior three months that the purchaser has sufficient net worth (such as bank statements and a consumer report) and obtaining a written representation from the purchaser that all liabilities necessary to make a determination of net worth have been disclosed; and
- receiving a written confirmation from a registered broker-dealer, SEC-registered investment adviser, licensed attorney or certified public accountant that such entity or person has taken reasonable steps to verify the purchaser's accredited status within the prior three months.

Issuers may continue to rely on Rule 506 to offer and sell securities to accredited and non-accredited investors, provided that they do not engage in any general advertising or general solicitation in offering and selling the securities. In addition, issuers that are conducting private offerings in reliance on Section 4(a)(2) outside of the Rule 506(c) exemption continue to be restricted in their communications and may not engage in general solicitation.

The final rules add a new check box to Form D for offerings made pursuant to the new Rule 506(c).

No Integration with Offshore Offerings

Regulation S provides a safe harbor for offers and sales of securities outside the United States and includes an issuer and a resale safe harbor. Two general conditions apply to both safe harbors: (1) the securities must be sold in an offshore transaction and (2) there can be no directed selling efforts in the US. Regulation S broadly defines "directed selling efforts" as: any activity undertaken for the purpose of, or that could reasonably be expected to have the effect of, conditioning the market in the US for any of these securities offered in reliance on Regulation S. Such activity includes placing an advertisement in a publication "with a general circulation in the US" that refers to the offering of securities being made in reliance upon Regulation S.

In the adopting release, the SEC states that, consistent with the historic treatment of concurrent Regulation S and Rule 506 offerings, concurrent offshore offerings under Regulation S will not be integrated with domestic unregistered offerings in which the issuer is relying on Rule 506(c) to engage in general solicitation.

Final Rules Disqualifying Bad Actors from Private Placements Under Rule 506

The SEC also approved final rules that preclude "bad actors" from relying on the exemption provided by Rule 506 of Regulation D. The exemption is not available if (among other persons) the issuer, any director, executive officer, or other officer participating in the offering has been convicted of, or is subject to court or administrative sanctions for, securities fraud or other violations of specified laws.

Proposed Rules

The SEC has also issued for public comment proposed rules that are intended to enhance the SEC's understanding of market practices in Rule 506 offerings and to address investor concerns related to the removal of the prohibition against general solicitation in Rule 506.

The proposed rules would require:

- the filing of a Form D in Rule 506(c) offerings no later than 15 calendar days prior to the first use of general solicitation or general advertising for such offering;
- providing additional information in a Form D filed in any Rule 506(c) offering concerning the issuer, the offered securities, the use of proceeds of the offering, the types of general solicitation that were used, and the methods used to verify investor status;
- the filing of a closing amendment to Form D no later than 30 calendar days after the termination of any Rule 506 offering;
- the inclusion in a prominent manner of certain legends and cautionary statements in written general solicitation materials used in Rule 506(c) offerings;
- the submission to the SEC no later than the date of first use of written general solicitation materials (on a temporary basis for two years); and
- the disqualification from relying on Rule 506 for one year if the issuer did not timely file Form D filing in a Rule 506 offering within the last five years.



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