



SEC Allows General Solicitation in Private Securities Offerings

07.29.2013

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As required by the JOBS Act, the SEC recently adopted final rules to allow general solicitation in certain private offerings. Issuers will now be permitted to use general solicitation (e.g., social media, newspapers and television) to offer unregistered securities as long as all sales of the security are made to “accredited investors” under new Rule 506(c) (the status of whom the issuer has reasonably verified) or to “qualified institutional buyers” under Rule 144A.

Amendment to Rule 506

Under new Rule 506(c), issuers must take reasonable steps to verify the accredited investor status of purchasers. Whether the steps taken are “reasonable” will be an objective determination by the issuer based on the particular facts and circumstances of each purchaser and transaction. Among the factors that issuers should consider are:

- the nature of the purchaser and the type of accredited investor that the purchaser claims to be;
- the amount and type of information that the issuer has about the purchaser; and
- the nature of the offering, such as the manner in which the purchaser was solicited, and the terms of the offering, such as a minimum investment amount.

The SEC also included a list of four non-exclusive methods to verify accredited investor status for natural persons. Issuers that use one of these verification methods will be deemed to have satisfied the requirement, provided the issuer has no knowledge that the purchaser is not accredited. Generally, the four methods are:

- *for investors who claim to be accredited based on their income*: reviewing copies of any Internal Revenue Service form that reports income (e.g., Form W-2, Form 1099, etc.) for the two most recent years, along with obtaining a written representation from the investor that he or she has a reasonable expectation of reaching the income level necessary to qualify as an accredited investor during the current year;

- *for investors who claim to be accredited based on their net worth:* reviewing one or more of the following types of documentation, dated within the prior three months, and by obtaining a written representation from the investor that all liabilities necessary to make a determination of net worth have been disclosed:
 - for assets: bank statements, brokerage statements and other statements of securities holdings, certificates of deposit, tax assessments and appraisal reports issued by independent third parties are deemed to be satisfactory; and
 - for liabilities: a credit report from at least one of the nationwide consumer reporting agencies is required.
- *for investors whose accredited status is confirmed by an independent professional:* obtaining a written confirmation from a registered broker-dealer, an SEC-registered investment adviser, a licensed attorney, or a certified public accountant that the independent professional has taken reasonable steps to verify that the investor is an accredited investor within the prior three months and has determined that the investor is accredited; or
- *for investors who have previously invested in the issuer as an accredited investor and who desire to invest in a new Rule 506(c) offering:* if a natural person (a) invested as an accredited investor in a Rule 506(b) offering by the issuer before the effective date of Rule 506(c) and (b) remains an investor of the issuer, the issuer will be deemed to have satisfied the verification requirement in Rule 506(c) with respect to that investor by obtaining a certification from the investor at the time of sale that the investor qualifies as an accredited investor.

Issuers will continue to have the ability under Rule 506 to conduct offerings without using general solicitation. As the SEC noted, it believes that offerings by issuers that do not wish to engage in general solicitation (and become subject to the verification requirements) or that wish to sell privately to non-accredited investors will represent an important source of capital for issuers of all sizes.

The SEC also noted that the amendments to Rule 506 affect only Rule 506, and not Section 4(a)(2) offerings in general. Therefore, even after the effective date of Rule 506(c), an issuer relying on Section 4(a)(2) outside of the Rule 506(c) safe harbor is prohibited from engaging in general solicitation.

Amendment to Rule 144A

The final rule makes a similar change to Rule 144A. The new rule allows securities sold under Rule 144A to be offered to persons other than qualified institutional buyers through means including general solicitation. Unlike the requirements under new Rule 506(c), the issuer does not have to verify the qualified institutional status of each purchaser, but must (as in Rule 506) reasonably believe that such purchaser is a qualified institutional buyer.

Proposed Amendments to Private Offering Rules

After adopting rules to permit general solicitation, the SEC proposed several amendments to the private offering rules that could impede on the usefulness of new Rule 506(c). Under the proposed rules, issuers that use general solicitation under Rule 506(c) would be:

- required to file an advance notice of sale on Form D 15 days before and at the conclusion of the offering;
- required to provide additional information about the issuer and the offering;
- disqualified from using Rule 506 for one year after its failure to file a Form D;

- required to include legends and disclosures in written general solicitation materials; and
- required to submit written general solicitation materials to the SEC no later than the date of first use.

Bad Actor Disqualification

The SEC also adopted a related final rule that prohibits an issuer from relying on Rule 506 (whether or not general solicitation is used) if the issuer or one of its directors, officers or certain large shareholders has a “disqualifying event.” A “disqualifying event” includes, but is not limited to, events such as criminal convictions, court injunctions, and restraining orders in connection with the purchase or sale of securities; SEC disciplinary orders, cease-and-desist orders, and stop orders; and suspension or expulsion for membership in a self-regulatory organization.

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