

Finally! SEC Approves Rule to Assist Companies Raising Capital

by Dan Brecher on July 25, 2013

As required by the JOBS Act, the Securities and Exchange Commission (SEC) finally enacted rules to allow for general solicitation of private security offerings. The move is good news for early stage and emerging companies, as it will open the door to billions of dollars in new funding.

The new rule specifically amends Rule 506 of Regulation D of the Securities Act of 1933. “Reg D” is the most commonly relied upon exemption to SEC registration and was responsible for more than \$1.3 trillion in funding in 2012.

Under the new rules, companies can use general solicitation and general advertising to offer securities pursuant to a Rule 506 offering, provided that all purchasers of the securities are accredited investors. Unlike other offerings exempt from registration under Regulation D, the issuer cannot simply take investors at their word, but must take reasonable steps to verify that the purchasers of the securities are accredited investors at the time of the sale of the securities. Potential advertising methods include newspapers, social media and radio advertisements.

The SEC’s final rule largely tracks what was first proposed last fall. However, in response to concerns regarding the steps issuers must take to verify that investors are “accredited,” the final rule includes a non-exclusive list of methods that issuers may use to satisfy the verification requirement for purchasers who are natural persons. They include:

- Reviewing copies of any IRS form that reports the income of the purchaser and obtaining a written representation that the purchaser will likely continue to earn the necessary income in the current year; 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.

In response to concerns about investor fraud, the SEC implemented additional amendments to Rule 506 to disqualify felons and other bad actors from relying on the exemption. Under the new rule, “disqualifying events” include criminal convictions, and court injunctions and restraining orders in connection with the purchase or sale of a security, as well as certain SEC stop orders, cease and desist orders, and disciplinary orders.

If you have any questions about the SEC's new rule or how it may impact your business, please contact me, Dan Brecher, or the Scarinci Hollenbeck attorney with whom you work.