JONES WALKER

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JUMPSTART OUR BUSINESS STARTUPS ACT – PART "DEUX": SEC ADOPTS RULES AUTHORIZING GENERAL SOLICITATION & ADVERTISING IN CONNECTION WITH CERTAIN PRIVATE OFFERINGS

On July 10, 2013, the Securities and Exchange Commission ("SEC") adopted new rules to implement Section 201(a) of the Jumpstart Our Business Startups Act, which was signed into law by President Obama in April 2012 ("JOBS Act").[1] The most noteworthy of the new rules *eliminated* the SEC's enduring, bedrock prohibition of the use of general solicitation and advertising by an issuer or its representatives in connection with certain exempt private offerings. In addition, the SEC issued a rule proposal to enhance Form D disclosure requirements.

These final and proposed rules are discussed in more detail below.

Adopted Final Rules

Amendments to Rules 506 and 144A

Rules 506 and 144A promulgated under the Securities Act of 1933 (the "Securities Act") are safe harbors from the registration requirements of the Securities Act for certain offerings and sales of securities. Specifically, Rule 506 (among other things) authorizes issuers to offer and sell an unlimited amount of securities without registration to an unlimited number of "accredited investors." Rule 144A permits the *resale* of an unlimited amount of restricted securities by non-issuers, underwriters, or dealers to "qualified institutional buyers" ("QIBs").

In a 4-1 vote, the new rules adopted by the SEC amends Rule 506 to add a new subsection Rule 506(c), which for the first time specially authorizes an issuer to use general solicitation and advertising in connection with an offering of their securities. Issuers utilizing this new safe harbor are, however, subject to certain stated conditions, including that the issuer takes "*reasonable steps to verify*" that the purchasers of the securities are accredited investors. Prior to the introduction of this enhanced verification standard, issuers offering its securities under the safe harbors provided by Rule 506 were required only to have a "reasonable belief" of the "accredited" status of its investors. While the reasonableness of the steps taken by the issuer to make such a principals-based method of verification is an objective determination based on the facts and circumstances of each offering, the final rule also provides a non-exclusive list of methods issuers may use to verify the status of individual accredited investors that, if utilized, will be *deemed* to satisfy these enhanced diligence requirements.

The non-exclusive verification methods adopted by the SEC include, without limitation, (i) reviewing copies of any IRS form reporting the income of the purchaser for the two most recent years, along with obtaining a written representation from such person that he or she has a reasonable expectation of reaching the income level necessary to qualify as an

[1] For additional information on the JOBS Act, passed on April 5, 2012, please see the Jones Walker E*Bulletin: *Jumpstart Our Business Startups Act: A New Horizon for Emerging Businesses*. Also see the *Jones Walker JOBS Act Resource Page*.

accredited investor during the current year; (ii) reviewing certain documents such as bank statements or brokerage accounts and obtaining a written representation from such person that all liabilities necessary to make a determination of net worth have been disclosed; or (iii) 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 investor status. In addition, the final rule amends Form D by adding a separate box for issuers to check to indicate whether the offering was conducted pursuant to Rule 506(c).

It is important to note that these amendments do not eliminate the right of an issuer to conduct an offering *without* the use of general solicitation in reliance on the safe harbors provided by Rule 506(b) and the "reasonable belief" standard contained in Rule 501(a) for determining when a purchaser is an accredited investor for purposes of all other Rule 506 exempt offerings.

In addition, the amendments to Rule 144A permit resale offers to persons other than QIBs, including through the use of general solicitation and advertising, where the securities are ultimately sold only to purchasers that the seller (or the person acting on the seller's behalf) reasonably believes are QIBs.

Notwithstanding concern expressed regarding the use of general solicitation by private funds leading up to the adoption of these final rules last week, the SEC confirmed that private funds would be able to engage in general solicitation without sacrificing the availability of certain exemptions under the Investment Company Act commonly relied upon by these organizations. However, the SEC did affirmatively state that it would continue to monitor and study the development of private fund advertising and undertake a review to determine whether any further action becomes warranted. Private funds also remain subject to separate rules under the Investment Advisors Act prohibiting the employment of fraudulent, deceptive, or manipulative acts in connection with their activities, and the final rules adopted by the SEC permitting the use of general solicitation by such private funds have no effect on such anti-fraud provisions.

The SEC's final rule lifting the general solicitation and advertising ban can be found here, and will become effective 60 days after publication of this rule-making in the *Federal Register*.

Disqualification of "Bad Actors"

In addition to the amendments to Rule 506 and Rule 144A described above, the SEC also adopted final rules prohibiting an issuer from relying on the Rule 506 exemption if the issuer or any other person covered by the rule had a "disqualifying event." Under the final rule, disqualifying events include, among others, (i) criminal convictions in connection with the purchase or sale of a security; (ii) making of a false filing with the SEC or arising out of the conduct of certain types of financial intermediaries and SEC disciplinary orders relating to brokers, dealers, and like parties; and (iii) SEC cease-and-desist orders related to violations of certain anti-fraud provisions and registration requirements of the federal securities laws.

The SEC's final rule disqualifying bad actors in connection with Rule 506 offerings can be found here.

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Proposed Rules

In addition to its final rules adopted on July 10, 2013, the SEC also proposed rules relating to Rule 506 which are intended to enhance the SEC's ability to assess developments in the private placement market, particularly given the adoption of the rules to lift the ban on general solicitation and advertising.

If adopted in the form proposed, the rules would, among other things, (i) require issuers to file an *advance notice* of sale on Form D, 15 days before engaging in a general solicitation for the offering and update the information within 30 days of completing the offering; (ii) require issuers to provide additional information on Form D relating to the issuer and the offering; (iii) disqualify issuers under certain circumstances from using the Rule 506 exemption; and (iv) require issuers to submit written general solicitation materials to the SEC through an intake page on the SEC's website.

The SEC stated that the proposal would also improve its ability to evaluate the development of market practices in Rule 506 offerings and would address certain concerns raised by investors related to issuers engaging in general solicitation.

The SEC's proposed rule relating to additional Form D amendments can be found here.

— Asher J. Friend and Raechelle M. Munna

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Remember that these legal principles may change and vary widely in their application to specific factual circumstances. You should consult with counsel about your individual circumstances. For further information regarding these issues, contact:

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