

Eliminating the Prohibition Against General Solicitation and General Advertising in Rule 506 and Rule 144A Offerings

A Small Entity Compliance Guide¹

Introduction

Enacted in 2012, the Jumpstart Our Business Startups Act, or JOBS Act, is intended, among other things, to reduce barriers to capital formation, particularly for smaller companies. The JOBS Act requires the SEC to adopt rules amending existing exemptions from registration under the Securities Act of 1933 and creating new exemptions that permit issuers of securities to raise capital without SEC registration. On July 10, 2013, the SEC adopted amendments to Rule 506 of Regulation D and Rule 144A under the Securities Act to implement the requirements of Section 201(a) of the JOBS Act. The amendments are effective on September 23, 2013.

Rule 506(b) of Regulation D

Section 4(a)(2) of the Securities Act exempts from registration “transactions by an issuer not involving any public offering.” Rule 506(b) is a rule under Regulation D that provides conditions that an issuer may rely on to meet the requirements of the Section 4(a)(2) exemption. One of these conditions is that an issuer must not use general solicitation to market the securities.

“General solicitation” includes advertisements published in newspapers and magazines, public websites, communications broadcasted over television and radio, and seminars where attendees have been invited by general solicitation or general advertising. In addition, the use of an unrestricted, and therefore publicly available, website constitutes general solicitation. The solicitation must be an “offer” of securities, but solicitations that condition the market for an offering of securities may be considered to be offers.

Rule 506(c) of Regulation D

Section 201(a) of the JOBS Act requires the SEC to eliminate the prohibition on using general solicitation under Rule 506 where all purchasers of the securities are accredited investors and the issuer takes reasonable steps to verify that the purchasers are accredited investors.

To implement Section 201(a), the SEC adopted paragraph (c) of Rule 506. Under Rule 506(c), issuers can offer securities through means of general solicitation, provided that:

- all purchasers in the offering are accredited investors,
- the issuer takes reasonable steps to verify their accredited investor status, and
- certain other conditions in Regulation D are satisfied.

[Return to Top](#)

An “accredited investor” includes a natural person who:

- earned income that exceeded \$200,000 (or \$300,000 together with a spouse) in each of the prior two years, and reasonably expects the same for the current year, or
- has a net worth over \$1 million, either alone or together with a spouse (excluding the value of the person’s primary residence).

An “accredited investor” may also be an entity such as a bank, partnership, corporation, nonprofit or trust, when the entity satisfies certain criteria. The full definition of “accredited investor” is available [here](#).

The JOBS Act requires that issuers wishing to engage in general solicitation take “reasonable steps” to verify the accredited investor status of purchasers. Rule 506(c) sets forth a principles-based method of verification which requires an objective determination by the issuer (or those acting on its behalf) as to whether the steps taken are “reasonable” in the context of the particular facts and circumstances of each purchaser and transaction. Among the factors that an issuer should consider under this principles-based method 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 to participate in the offering, and the terms of the offering, such as a minimum investment amount.

In addition to this flexible, principles-based method, Rule 506(c) includes a non-exclusive list of verification methods that issuers may use, but are not required to use, when seeking greater certainty that they satisfy the verification requirement with respect to natural person purchasers. This non-exclusive list of verification methods consists of:

- verification based on income, by reviewing copies of any Internal Revenue Service form that reports income, such as Form W-2, Form 1099, Schedule K-1 of Form 1065, and a filed Form 1040;
- verification on net worth, by reviewing specific types of documentation dated within the prior three months, such as bank statements, brokerage statements, certificates of deposit, tax assessments and a credit report from at least one of the nationwide consumer reporting agencies, and obtaining a written representation from the investor;
- a written confirmation from a registered broker-dealer, an SEC-registered investment adviser, a licensed attorney or a certified public accountant stating that such person or entity has taken reasonable steps to verify that the purchaser is an accredited investor within the last three months and has determined that such purchaser is an accredited investor; and
- a method for verifying the accredited investor status of persons who had invested in the issuer’s Rule 506(b) offering as an accredited investor before September 23, 2013 and remain investors of the issuer.

Rule 506(b) remains unchanged following the adoption of Rule 506(c) and continues to be available for issuers that wish to conduct a Rule 506 offering without the use of general solicitation or that do not wish to limit sales of securities in the offering to accredited investors.

Rule 144A is a non-exclusive safe harbor exemption from the registration requirements of the Securities Act for resales of certain securities to qualified institutional buyers, or QIBs. A QIB includes certain entities that, in the aggregate, own and invest on a discretionary basis at least \$100 million in securities of unaffiliated issuers. A registered broker-dealer qualifies as a QIB if it owns and invests on a discretionary basis at least \$10 million in securities of unaffiliated issuers. Prior to the recent amendment to Rule 144A described below, offers of securities under Rule 144A were required to be limited to QIBs, which effectively prohibited the use of general solicitation under Rule 144A.

Section 201(a) of the JOBS Act requires the Commission to revise Rule 144A to provide that securities sold pursuant to Rule 144A may be offered to persons other than QIBs, including by means of general solicitation, provided that securities are sold only to persons that the seller and any person acting on behalf of the seller reasonably believe are QIBs. To implement Section 201(a), the SEC adopted an amendment to Rule 144A to permit the use of general solicitation under Rule 144A, as long as the purchasers are limited to QIBs or to purchasers that the seller and any person acting on behalf of the seller reasonably believe are QIBs.

Other Resources

The adopting release for the amendments to Rule 506 and Rule 144A can be found on the SEC's website at <http://www.sec.gov/rules/final/2013/33-9415.pdf>.

Rule 506 and Rule 144A can be accessed through the "Corporation Finance" section of the SEC's website at <http://www.sec.gov/divisions/corpfin/ecfrlinks.shtml>.

Additional materials regarding the application of Rule 506 and Rule 144A are available at <http://www.sec.gov/divisions/corpfin/cfguidance.shtml>.

You can also submit complaints or tips about possible securities laws violations on the SEC's questions and complaints page at <http://www.sec.gov/complaint.shtml>.

Contacting the SEC

The SEC's Division of Corporation Finance is happy to assist small companies with questions regarding the amendments to Rule 506 and Rule 144A. You may contact the Division's Office of Chief Counsel for this purpose at https://www.sec.gov/forms/corp_fin_interpretive or by telephone at (202) 551-3500. Questions on other corporate finance matters concerning small companies may be directed to the Division's Office of Small Business Policy through the above [online form](#) or by telephone at (202) 551-3460.

¹ This guide was prepared by the staff of the U.S. Securities and Exchange Commission as a "small entity compliance guide" under Section 212 of the Small Business Regulatory Enforcement Fairness Act of 1996, as amended. The guide summarizes and explains rules adopted by the SEC, but is not a substitute for any rule itself. Only the rule itself can provide complete and definitive information regarding its requirements.

Modified: Sept. 20, 2013

 [Return to Top](#)