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SEC Amends Rules 506 and 144A to Permit General Solicitation and Advertising in Unregistered Securities Sales

As directed by the Jumpstart Our Business Startups (JOBS) Act, enacted in 2012, the Securities and Exchange Commission recently adopted amendments to Securities Act Rules 506 and 144A, to permit general solicitation and advertising in connection with unregistered sales of securities, in limited circumstances.

Rule 506, a safe harbor exemption from registration for offers and sales of securities by an issuer not involving any public offering, previously prohibited general solicitation and advertising, for example, in newspapers, on radio or TV, or over the Internet. As amended, the rule permits general solicitation and advertising if sales of the securities are limited to accredited investors and the issuer has taken "reasonable steps to verify" that the purchasers are accredited investors. In the SEC's view, an issuer taking reasonable steps to verify that a purchaser is an accredited investor does not lose the exemption by selling to a non-accredited investor that falsely claimed to be accredited.

Whether the issuer has taken reasonable steps depends on the facts and circumstances in each case, including the category of accredited investor the purchaser claims to be, the information about the purchaser available to the issuer, and the nature and terms of the offering. An issuer would not be entitled to rely on only a check-the-box response by an investor.

The amended rule describes four non-exclusive, non-mandatory methods of verifying an individual's status as an accredited investor:

Basis for establishing status	Documentation
Income	IRS reporting forms, including W-2, 1099, K-1, and Form 1040, for previous two years, and written representation by purchaser regarding current year
Net worth	Bank, brokerage statements, tax assessments, third-party appraisals regarding assets, and credit report from national agency regarding liabilities, each dated within last three months; and written representation by purchaser that all liabilities have been disclosed
Third-party confirmation	Written confirmation from registered broker-dealer or investment adviser, attorney, or CPA of purchaser's accredited investor status within last three months
Pre-amendment investor	With respect to post-amendment offerings using general solicitation or advertisement, issuer may rely on written representation of accredited investor in issuer's pre-amendment offering that investor continues to be accredited

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Companies may continue to sell securities without general solicitation or advertising under Rule 506 to persons who are or are “reasonably believe[d]” to be accredited investors and to a limited number of non-accredited investors. Form D is being amended so that a company filing the form in connection with a Rule 506 offering will indicate whether the offering is made with or without general solicitation.

Pursuant to the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, the SEC also amended Rule 506 to make it unavailable to an issuer (regardless whether general solicitation is used) if, after the effective date of the amendment, the issuer or a related party is convicted of a crime or becomes subject to a court or regulatory order relating to violations of securities, banking, or insurance law or mail fraud. Issuers conducting a Rule 506 offering must disclose any of these events occurring before the effective date of the amendment.

The SEC also amended Rule 144A, a safe harbor for unregistered resales of securities, to permit general solicitation and advertising of Rule 144A offerings, as long as sales are limited to persons reasonably believed to be qualified institutional buyers.

The amendments become effective September, 2013.

Concurrent with these amendments, the SEC proposed additional amendments to regulations relating to Rule 506 offerings to:

- Require a Form D notice of sale to be filed at least 15 days before using any general solicitation;
- Require filing a closing amendment to Form D after completing a Rule 506 offering;
- Prohibit reliance on Rule 506 for offerings following an offering for which Form D was not filed;
- Require additional information in Form D;
- Require legends in Rule 506 general solicitation material;
- Regulate private fund Rule 506 general solicitation material; and
- Temporarily require submission to the SEC of Rule 506 general solicitation material.

Loeb & Loeb LLP's Capital Markets Department

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Capital Markets Department

VIVIEN (YUN) BAI	VBAI@LOEB.COM	+86 10 5954 3557
NORWOOD P. BEVERIDGE, JR.	NBEVERIDGE@LOEB.COM	212.407.4970
GREGORY J. BLASI	GBLASI@LOEB.COM	212.407.4236
GIOVANNI CARUSO	GCARUSO@LOEB.COM	212.407.4866
DEBORAH CHENG	DCHENG@LOEB.COM	+852 3923 1116
GERALD M. CHIZEVER	GCHIZEVER@LOEB.COM	310.282.2121
ROY CHOI	RKCHOI@LOEB.COM	+852 3923 1138
ROBERT CHUNG	RCHUNG@LOEB.COM	310.282.2216
STEPHEN H. COHEN	SCOHEN@LOEB.COM	212.407.4279
JOSEPH F. DANIELS	JDANIELS@LOEB.COM	212.407.4044
ANGELA M. SANTORO DOWD	ADOWD@LOEB.COM	212.407.4097
ALLAN B. DUBOFF	ADUBOFF@LOEB.COM	310.282.2141
ROSS D. EMMERMAN	REMMERMAN@LOEB.COM	312.464.3357
DAVID C. FISCHER	DFISCHER@LOEB.COM	212.407.4827
STEVEN E. HURDLE, JR.	SHURDLE@LOEB.COM	310.282.2187
CHRISTOPHER J. KELLY	CKELLY@LOEB.COM	310.282.2263
SUSIE L. KIM	SLKIM@LOEB.COM	212.407.4933
WALLACE LAU	WLAU@LOEB.COM	+852 3923 1128
FRANK LEE	FLEE@LOEB.COM	212.407.4825
STEPHEN LEUNG	SLEUNG@LOEB.COM	+852 3923 1134

DAVID J. LEVINE	DLEVINE@LOEB.COM	212.407.4923
GUOHUA LI	GLI@LOEB.COM	212.407.4927
JASZICK MALDONADO	JMALDONADO@LOEB.COM	212.407.4897
COREY N. MARTIN	CMARTIN@LOEB.COM	212.407.4841
BARRY T. MEHLMAN	BMEHLMAN@LOEB.COM	212.407.4812
C. CHRISTOPHER MURILLO	CMURILLO@LOEB.COM	212.407.4168
MITCHELL S. NUSSBAUM	MNUSSBAUM@LOEB.COM	212.407.4159
BENNY PANG	BPANG@LOEB.COM	+852 3923 1198
SIMONA S. PAPAIZIAN	SPAPAIZIAN@LOEB.COM	212.407.4941
ROGER C. PENG	RPENG@LOEB.COM	+86 10 5954 3552
RONELLE C. PORTER	RPORTER@LOEB.COM	212.407.4110
DAVID S. SCHAEFER	DSCHAEFER@LOEB.COM	212.407.4848
FRAN M. STOLLER	FSTOLLER@LOEB.COM	212.407.4935
ALLEN Z. SUSSMAN	ASUSSMAN@LOEB.COM	310.282.2375
LILI TAHERI	LTAHERI@LOEB.COM	212.407.4160
LAWRENCE VENICK	LVENICK@LOEB.COM	+86 10 5954 3688
XIKANG WANG	XWANG@LOEB.COM	+86 10 5954 3556
TIMOTHY WONG	TWONG@LOEB.COM	+852 3923 1136
TAHRA T. WRIGHT	TWRIGHT@LOEB.COM	212.407.4122
CONNIE YU	CYU@LOEB.COM	+852 3923 1126