

SMITH ANDERSON

Client Alert

Expect Excellence

January 2013

We're Still Waiting: When Will the SEC Lift the Ban on General Solicitation and Advertisements for Rule 506 and 144A Offerings?

Title II of the "Jumpstart Our Business Startups" Act ("JOBS Act"), which became law on April 5, 2012, aims to provide more flexibility for private company fundraising by eliminating the prohibition on general solicitation or advertising for "private" offerings made to accredited investors under Rule 506 of Regulation D and for secondary sales made to qualified institutional buyers ("QIBs") under Rule 144A.

Rules Lifting Ban on General Solicitation: Congress stipulated that the Securities and Exchange Commission ("SEC") adopt rules that require sellers engaging in general solicitation to take "reasonable steps" to verify that all purchasers are accredited investors or QIBs. Congress gave the SEC a deadline of July 2012 to implement these rules, however, the agency has thus far failed to complete its task. Until the SEC adopts final rules and declares them effective, the ban on general solicitation and advertising in Rule 506 and 144A offerings remains in place.

Lifting the ban on general solicitation is one of the most significant, and highly anticipated, of the many regulatory reforms undertaken by the JOBS Act. However, the agency has been slow to act. It issued proposed rules in late August and the 30-day comment period has come and gone. So, it appears likely that this aspect of the JOBS Act may remain "in limbo" while we welcome in the New Year.

Overview of Proposed Rules: The rules implementing Title II of the JOBS Act, as currently proposed by the SEC, are not without controversy. The SEC elected not to provide a list of specific methods by which a seller could satisfy the verification requirement, noting that proposing such methods could be overly burdensome in some cases and ineffective in others. Instead, the agency indicated that the verification process should involve an objective determination, based on the particular facts and circumstances of each transaction. (We do note that the proposed rules retain the current so-called "quiet" Rule 506 offering, the safe harbor under which companies may conduct Rule 506 offerings without the use of general solicitation.)

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While some commentators applaud the SEC for providing sellers “flexibility” to conduct their offerings, others view the SEC as having “punted” on its prime directive--that of providing sellers a solid regulatory framework and clear understanding of the verification procedures that will satisfy the statutory requirements. In addition, the SEC has come under fire for “misconstruing” the intent of the JOBS Act by permitting all issuers (including, in particular, private investment vehicles) to take advantage of the relaxed general solicitation requirements. In his comments to the SEC, Senator Carl Levin (D-MI), insists that the removal of the ban on general solicitation was intended solely for operating companies and not for hedge funds or other private investment vehicles.

We’re Still Waiting: It remains to be seen how the SEC will react to these and other comments and whether it may change its position on the scope of Title II or provide more clarity on what purchaser qualification verification steps would, with certainty, be deemed sufficiently “reasonable” under the new rules. More importantly, we cannot predict with any certainty when final rules will be issued. Until we get more clarity from the SEC, the ban on general solicitation remains in place and it simply remains a waiting game.