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NASAA

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Submitted electronically to rule-comments@sec.gov

Elizabeth M. Murphy
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

RE: NASAA Comments in Response to Release Nos. 33-9416, 34-69960, IC-30595 (File No. S7-06-13), "Amendments to Regulation D, Form D and Rule 156 under the Securities Act"

Dear Ms. Murphy,

The North American Securities Administrators Association, Inc. (NASAA) submits the following comments in response to Release Nos. 33-9416, 34-69960, and IC-30595 regarding proposed amendments to Regulation D, Form D, and Rule 156. We suggested several improvements to Regulation D in our comment letter dated October 3, 2012, in response to the Commission's proposal to lift the ban on general solicitation in Rule 506 (Release No. 33-9354, File No. S7-07-12), and we are pleased to see many of our suggestions reflected in the current proposal.

As you know, the members of NASAA are the state-level securities regulators who partner with the Commission in policing the private offering marketplace. As the regulators who are closest to small investors throughout the United States, we frequently receive complaints from those who are victimized in offerings conducted under Rule 506. In 2011 and 2012, Rule 506 offerings ranked as the most common product or scheme leading to enforcement actions by state securities regulators. Indeed, in those two years alone, NASAA members recorded 340 enforcement actions involving Rule 506 offerings, and private placements are commonly listed on our annual list of top investor traps. [1]

In addition to working to protect Main Street investors, state regulators frequently educate Main Street businesses about alternatives for raising capital under state and federal law, including Rule 506. We want to see those businesses succeed in their capital formation efforts so they can thrive and create jobs in our local communities. No NASAA member is

[1] See *Laws Provide Con Artists with Personal Economic Growth Plan: NASAA Identifies Emerging and Persistent Investor Threats* (August 21, 2012), available at http://www.nasaa.org/14679/laws-provide-con-artists-with-personal-economic-growth-plan/.

interested in creating excessive or inefficient rules, but we have learned that efforts to spur successful capital formation must reflect a balanced regulatory approach that minimizes unnecessary costs and burdens on small businesses while protecting investors from fraud and abuse. Without adequate investor protections to safeguard the integrity of the private placement marketplace, investors should and will flee from the market, depriving small businesses of an important source of capital.

NASAA strongly believes that modest changes can be made to Rule 506 and Form D that will enhance the ability of the Commission and NASAA members to protect investors while minimizing the burdens to the small businesses who utilize the rule to raise capital. These changes need to be adopted quickly, before unmonitored general solicitations begin to erode investor confidence in private placements and make it harder for businesses to find investors who are willing to enter this marketplace.

I. The Commission should require the filing of Form D prior to the use of general advertising.

Question #8 in the proposing release specifically asks "How would state securities regulators use the Advance Form D filings?"[2] As explained in our prior comment letter, the Form D is an important tool to the states in our efforts to inform and protect investors. Thus, it is essential for state regulators and prospective investors to have access to the information disclosed in Form D at or before the time an issuer begins to advertise to the general public.

As part of our investor education efforts, state regulators implore investors to "investigate before you invest," and we encourage investors to contact the securities regulators in their states if they have questions about an offering. Frequently asked questions include whether the offering is registered or exempt, whether there have been any complaints against the issuer or placement agents, and whether the issuer, control persons, or placement agents have any regulatory history. With the Commission's recent lifting of the ban on general solicitation, we anticipate a substantial increase in the number of investors who will want this type of information. However, without a requirement that the Form D be filed prior to the use of general solicitation, there is no way for state securities regulators to respond to these basic questions. An investor that contacts a state securities regulator to ask about an offering is simply being diligent, and state regulators should have the information necessary to respond to such inquiries.

In addition, the lack of a pre-solicitation filing makes it impossible for state enforcement personnel to easily determine whether an offering is being conducted in accordance with the securities laws. Under the current rules, Form D need not be filed until 15 days after the first *sale*, so an issuer can advertise for investors without filing the form. An

[2] Question #28 asks a similar question: "Would the additional information that we propose to request in Form D provide useful information to state securities regulators in responding to inquiries from constituents about offerings conducted under Rule 506 and in enforcement efforts?" As described more fully below, the answer is an emphatic "yes."

investigator who sees an advertised offering will not be able to check the Commission's records to quickly determine whether the issuer is attempting to engage in a compliant Rule 506(c) offering or is merely advertising an unregistered, non-exempt public offering with no intention of complying with any legal requirements. Federal enforcement personnel, including Commission staff and federal law enforcement officials, will face a similar uncertainty. Regulators may have no alternative except to contact issuers – with subpoenas, if necessary – to determine whether their offerings are being conducted in compliance with Rule 506(c). This will increase the number of investigative inquiries directed to legitimate issuers and lengthen the process for stopping illegitimate offerings. Ultimately, investors will be put at greater risk because it will be more difficult for regulators to prevent or stop investor losses.

We note that the proposed rule would require the filing of Form D fifteen days before an issuer engages in general solicitation. We do not believe a fifteen day advance filing requirement is unduly burdensome to an issuer who wishes to seek investments from the general public. However, for our purposes it would be sufficient to simply require the filing at any time prior to the use of general advertising. The critical issue is that the Form D should be publicly accessible before an issuer begins to publicly solicit investors.

II. The Commission should establish meaningful consequences for those who fail to file Form D.

For far too long, the Commission has failed to address a glaring problem in Rule 506 offerings. As reported by the SEC Inspector General in 2009, "there are simply no tangible consequences when a company fails to file a Form D." [3] The proposing release cites to only one case in which the Commission has ever brought an action under Rule 507 to enjoin an issuer from future use of Regulation D.

The voluntary nature of Form D has significant repercussions for state regulators. Pursuant to Section 18 of the Securities Act of 1933, states are preempted from requiring registration of securities that are sold in compliance with Rule 506. However, state regulators routinely review Form D filings to ensure that the offerings actually qualify for an exemption under Rule 506 and to look for "red flags" that may indicate a fraudulent offering. The absence of a Form D filing complicates our efforts to protect the investing public. In addition, a promoter who has no intention of complying with Rule 506 may attempt to assert it as a defense to a state-level enforcement action by filing a Form D long after the fact.

[3] SEC Inspector General Report No. 459, "Regulation D Exemption Process" (March 31, 2009), at 10, available at http://www.sec-oig.gov/Reports/AuditsInspections/2009/459.pdf. When Rule 506 was originally adopted in 1982, it required compliance with Rules 501 through 503, including the timely filing of a Form D, in order to qualify for the exemption. 47 Fed. Reg. 11251, 11267 (Mar. 16, 1982). In 1989, Regulation D was amended to remove the requirement of compliance with Rule 503 as a condition of the Rule 506 exemption. 54 Fed. Reg. 11369, 11373 (Mar. 20, 1989). The Commission's summary of the rule change stated, "While the filing of Form D has been retained, it will no longer be a condition to any exemption under Regulation D. New Rule 507 will disqualify any issuer found to have violated the Form D filing requirement from future use of Regulation D." SEC Release No. 6,825 (Mar. 14, 1989).

Apart from bad actors, it is likely that many legitimate issuers never file a Form D because they simply have no incentive to file one. As the proposing release illustrates, this makes it nearly impossible to accurately gauge the size of the private placement market.[4] From what we do know, the market rivals the size of public offerings, but policy-makers are left to guess at the implications of loosening the rules for private placements. The information captured in Form D, as enhanced in the proposing release, will provide important data that can be used to determine future economic impacts for businesses and investors. A lack of a true and complete understanding of the private placement market hampers our ability to foster growth in that market and police bad actors.

We do not believe it is likely that an issuer will "accidentally" fail to file the Form D, particularly when an issuer is intentionally trying to avail itself of the new exemption in 506(c) to engage in broad public advertising for investors. If an issuer is engaged in an advertising campaign, taking reasonable steps to verify whether investors are accredited, and selling only to accredited investors, it is difficult to believe that the issuer would innocently forget to file the required form.

For these reasons, it is imperative for the Commission to act quickly to establish meaningful consequences for issuers who fail to file a Form D. Because the filing is such a critical part of the exemption, and because it is such a simple condition to satisfy, we believe that the loss of the exemption is a reasonable consequence for failure to file the form. The only appropriate cure for a late filing is a rescission offer.

III. The content of Form D should be enhanced to capture data that is important to the Commission and investors.

In our prior comment letter, we requested the addition of several data points to Form D, several of which are reflected in the proposed Advance Form D. For example, you would require a website address for the issuer, identification of certain control persons, and the identification of any adviser to a pooled fund, and we continue to strongly support these changes. Other amendments advocated by NASAA were also included in the recent final rules related to Rule 506, such as the requirement to indicate whether general solicitation is used and a certification that the offering is not disqualified due to "bad actors."

NASAA fully supports the proposed disclosure of certain uses of proceeds because it will provide clear, material information that is necessary for investors to make informed decisions and will make it harder for fraudsters to cover their tracks in cleverly worded offering documents. We also support the proposal to include on the Form D an indication of the verification method used. In addition, while we previously requested that you eliminate the

[4] A study by the SEC's chief economist in 2011 found that private offerings grew by nearly 50% from 2009 to 2010; from about $950 billion to about $1.4 trillion, and that private stock issuances surpassed debt issuances in 2010 and the first quarter of 2011. See Craig Lewis, "Unregistered Offerings and the Regulation D Exemption," November 2, 2011, available at http://www.sec.gov/info/smallbus/acsec/acsec103111presentation-regd.pdf.

option for declining to disclose issuer size, we are satisfied with your proposal to replace "decline to disclose" with "not public" if the information is not already in the public domain.

We continue to believe, however, that it would be beneficial to require the issuer to indicate whether it has sold or may sell to non-accredited investors, whether those investors are sophisticated, whether it has created an offering circular, and whether non-accredited investors have been provided with the same information that is available to accredited investors. The Commission should also include a checkbox on Form D to indicate that the issuer is required to provide disclosure of prior "bad actor" events under Rule 506(b)(2)(iii). These common-sense proposals would help investors and regulators quickly determine whether the offering is being conducted properly. In addition, it would be useful to require a CUSIP number, a consent to venue as well as service of process, plus a warning that finders' fees may trigger state and federal salesperson and broker-dealer registration requirements.

On balance, the enhancements you have proposed to Form D are significant steps in the right direction, and we encourage swift adoption of the proposed form. We encourage you to make the changes applicable to both 506(b) and 506(c) offerings so the data is consistent and one form can be used for all offerings conducted under Rule 506.

IV. The Commission should require the filing of a closing amendment to Form D.

In previous comment letters, NASAA has encouraged the Commission to require a post-offering filing of a closing Form D in order to allow the Commission and state regulators to track the use of the exemption. We appreciate the inclusion of this requirement in the proposing release and continue to advocate for its adoption for offerings conducted under both 506(b) and 506(c). Even if no sales are actually made, a closing amendment should be required so that the Commission captures important data about offerings that were unsuccessful and the types of issuers who have difficulty raising capital. This data will be an absolute necessity in determining whether the changes to Regulation D were effective in achieving the JOBS Act goals of economic growth and job creation or whether investors are reluctant to invest in these offerings.

We do not believe the failure to file a closing amendment should result in the loss of an exemption for an offering that has already occurred in reliance upon the exemption. However, the Commission should establish a process for reminding issuers of their obligation to file closing amendments. In addition, the Commission should establish meaningful penalties for failure to make a timely filing, such as a one year ban from using Rule 506.

V. In lieu of lengthy advertising legends, the Commission should adopt more meaningful measures to ensure that appropriate disclosures are made to investors.

In our view, it is not necessary for the Commission to require the long advertising legend in proposed Rule 509. We agree that the issuer should be required to disclose the information that is contained in the proposed legend, but it would be better for the Commission

to require some indication that the issuer has read the material. This could be done by requiring the information to be contained in the subscription agreement or by requiring the investor to click through the information on the issuer's chosen internet platform.

VI. The Commission should require the use of a very brief legend that allows the Commission to monitor on-line advertising.

Instead of the lengthy legend as proposed, the Commission should require a very brief legend on all internet-based general solicitations. A brief legend containing a unique short phrase will readily identify the offering as one being conducted under Rule 506 and make it easy for the Commission to monitor on-line advertising. For example, a tag such as "506OfferingX," where X represents the Central Index Key (CIK) number for the issuer or the SEC File Number for the related Form D filing, would make it easy for Commission staff to search for advertising materials related to a particular offering. Even something as simple as "#506" may be sufficient.

If the Commission adopted a short tag of this nature, it may not be necessary to impose a temporary filing requirement for on-line advertising materials that contain the required legend. Rule 510T could then be narrowed to require only the filing of other types of advertisements. However, to accomplish the purpose of replacing the filing requirement with searchable advertisements, the Commission must adopt explicit technical requirements for internet-based solicitations and update those requirements as technology progresses. Initially, we suggest that the Commission should require internet-based solicitations to be conducted only on websites with compliant sitemap XML files that do not contain robots.txt files. The tag should be included in the website as plain HTML and not as an image, Flash, or by dynamic generation from a database. The tag should also be placed in the Title HTML tag for the website, the footer, or some other prominent portion of the website. It should not be placed in hidden content on the website such as an HTML comment.

NASAA believes there will be fewer incidents of fraud and deceptive advertising practices if the materials are required to be filed with the Commission or are subject to easy inspection by regulators. NASAA encourages the Commission to adopt robust measures to protect investors from unscrupulous advertising while taking advantage of technology to minimize the costs to legitimate issuers.

VII. The Commission should place reasonable restrictions on the advertising that is used under Rule 506.

In our prior comment letter, we asked the Commission to place restrictions on private fund advertising that are comparable to the rules for mutual funds. Otherwise, private funds subject to very little regulation would be able to compete against more rigorously regulated mutual funds for investors, even though the investment strategies of private funds are typically more opaque, risky, and illiquid than those of mutual funds. To even the playing field, we called upon the Commission to subject private fund advertisements to restrictions that are

comparable to the rules for mutual funds, including Rule 482 (performance advertising), Rule 156 (prohibiting misleading advertising), and Rule 206-4(8) (prohibiting deceptive or manipulative practices). We are pleased that the proposing release reflects many of our concerns and suggestions, but the final rule could be improved with the addition of more stringent safeguards to limit performance advertising.

While we are pleased that the proposing release addresses advertising by private funds, we are concerned that it fails to provide guidance to other types of issuers. Entrepreneurs are understandably optimistic when it comes to their ventures, which could easily lead to exaggerations and misstatements giving rise to liability when done in the context of a securities offering. To minimize this risk, issuers need guidance to help them properly exercise their duty to disclose material facts to prospective investors. At a minimum, Rule 509 should require all issuers, not just private funds, to make a balanced presentation of risks and rewards. Furthermore, the rule should require that all statements in advertising are consistent with representations in the offering documents.[5]

VIII. The Commission should update the Accredited Investor definition to ensure that it more accurately reflects investor sophistication.

NASAA recognizes that the Commission's ability to redefine the accredited investor standards may be restricted by Section 413 of the Dodd-Frank Act. However, NASAA encourages the Commission to revisit the monetary thresholds set forth in the "accredited investor" definition in Rule 501 to account for inflation that has occurred since the rule's adoption. According to the U.S. Bureau of Labor Statistics, $200,000 had the same buying power in 1982 as $484,719 has in 2013,[6] but the annual income threshold for accredited investors remains unchanged. Similarly, $1,000,000 had the same buying power in 1982 as $2,423,595.85 today,[7] yet the net worth threshold has only been changed during that time period to remove the value of a potential investor's primary residence from the calculation.

We agree with the GAO report that dollar thresholds have never been an accurate proxy for investor sophistication. Additionally, Section 4(2) case law has never recognized wealth as a reliable indicator of investor sophistication. We believe it is time to shift away from wealth as the sole determinant of accredited investor status, and we call upon the Commission to adopt a definition that reflects true investor sophistication. However, given the importance of the other rules that have been proposed in the current release, we urge the Commission to move forward with the other rule proposals and to address the accredited investor definition in a separate rulemaking.

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[5] In December 2011, the Commission released "CF Disclosure Guidance: Topic No. 3," which provides guidance regarding the review of promotional and sales material in registered offerings. See http://www.sec.gov/divisions/corpfin/guidance/cfguidance-topic3.htm. Rule 506 offerings should be required to adhere to many of those same standards.

[6] *See* http://www.bls.gov/data/inflation_calculator.htm as of September 18, 2013.

[7] *Id.*

IX. The Commission should evaluate the costs and benefits of all changes to Rule 506 together, not in isolation.

Overall, NASAA supports the proposed rules because they would put in place important protections for investors with minimal burdens for issuers. However, we are greatly disappointed that the Commission elected to move forward on lifting the ban on general solicitation for private offerings while choosing to delay these related investor protections. Now, opponents of these modest changes will likely argue that the proposed rules are costly and burdensome, as though they did not just receive the enormous benefits from the elimination of the ban on general solicitation.

The proposing release states that "we are proposing today a number of amendments *in conjunction with* the adoption of new Rule 506(c)."[8] This indicates that the costs and benefits of the current proposals should be evaluated in conjunction with the earlier changes. Former Commissioner Walter expressed a similar view, stating that "[w]hile I'm pleased to support all three releases, *I would like to make it clear that I view them as a package*."[9] We urge the Commission to consider the proposed rules as further adjustments that were necessitated by the lifting of the general solicitation ban, not as isolated changes that are evaluated independent of the earlier amendments.

Conclusion

The recent changes to Rule 506 will have an enormous impact on the securities markets in the United States. While some of those impacts will be positive, we can anticipate that a greater number of investors will be defrauded, sold unsuitable investment products, or otherwise victimized in offerings conducted under Rule 506. We believe that it is imperative for the Commission to adopt reasonable rules to protect investors in this market and that improvements to Rule 506 will facilitate the investor trust that is necessary to promote the capital formation goals embodied in the JOBS Act.

We have suggested modest changes to the proposed rules that we believe will yield important protections for investors at the lowest possible cost to issuers, and we have pointed out places where the proposed rules could be scaled back to save costs without unduly harming investors. *It is our hope that this balanced approach will help the Commissioners reach consensus on these issues so that the final rules will be adopted as rapidly as possible.*

It is also our hope that the Commission staff who are involved in the "Rule 506(c) Work Plan" will collaborate with state securities regulators. As your partners in the protection

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[8] See Release Nos. 33-9416, 34-69960, and IC-30595, p. 10 (emphasis added).

[9] Elisse B. Walter, Opening Remarks Regarding the Adoption of Rules Eliminating the Prohibition Against General Solicitation, the Adoption of Rules Regarding Disqualification of "Bad Actors" from Rule 506 Offerings, July 10, 2013.

of investors and fostering responsible capital formation, we can be a valuable resource in monitoring developments in the Rule 506(c) marketplace.

If you would like further information or clarification, please contact me or NASAA's Deputy General Counsel, Rick A. Fleming, at (202) 737-0900.

Sincerely,

A. Heath Abshure
President