

Advertising Under Rule 506: A Two-Edged Sword

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It is not necessarily advisable for issuers to take advantage of a recent SEC rule amendment – required by last year’s “JOBS Act” -- that permits general solicitation or advertising (collectively, “general solicitation”) in connection with private offerings under Rule 506 of the SEC’s Regulation D. Of course, general solicitation often could enable issuers to reach a larger number of potential investors and to avoid often cumbersome procedures that historically have been necessary to ensure the general solicitation would not be deemed to have been used. However, using general solicitation will require the issuer in a Rule 506 offering to:

- forego the opportunity to sell the offering to any investors who are not “accredited.” This may become more important to the extent that, as is likely, the SEC in the future raises the requirements for being “accredited”;
- take “reasonable steps” to verify each purchaser’s accredited status that in many cases will need to go well beyond the process by which investors historically have simply “self-certified” that they meet one of the standards for being accredited;
- forgo the possibility of falling back on the traditional (non-Regulation D) private offering exemption as a back stop in case the issuer inadvertently fails to satisfy any of the conditions for availability of Rule 506. This can expose issuers to additional risk, particularly because the amendments that the SEC has recently adopted or is currently contemplating are likely to complicate Regulation D in ways that can substantially increase the risk of such an inadvertent failure (see ““Bad Actors” Barred from Rule 506 Private Placements” on page 14); and
- check a special box on its Form D filing, which could very well prompt intense scrutiny by various state and federal regulatory bodies, who already have expressed keen interest in general solicitation activities. At a minimum, issuers will have ample reason to scrupulously avoid any materially inaccurate, incomplete or misleading solicitations.

Moreover, the SEC has proposed a number of potentially troublesome additional requirements under Regulation D that would apply only to issuers making a general solicitation; and it is not certain to

what extent such requirements, if adopted, might be triggered, for example, by the continuation of offerings that had already commenced using general solicitation. Finally, use of general solicitation may in some cases result in less favorable treatment for certain purposes under state and non-U.S. securities laws and CFTC regulations.

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