U.S. Securities and Exchange Commission

Facilitating General Solicitation at the Expense of Investors

by

Commissioner Luis A. Aguilar

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Today, among other things,[1] the Commission considers amendments to Rule 506 of Regulation D, to remove the prohibition against general solicitation and advertising, if sales are made only to accredited investors.[2] I do not support this action because both the process followed in proposing the amendments and the actual amendments being considered today come at the expense of investors and place investors at greater risk. I am particularly disappointed because this flies in the face of the Commission's mission and did not have to be the case.

The Commission has both the Authority and the Obligation to Protect Investors in Implementing JOBS Act Section 201

Last year, Congress passed the Jumpstart Our Business Startups Act ("JOBS Act").[3] Section 201(a) of the JOBS Act requires the Commission to revise Rule 506 to remove the prohibition against general solicitation and general advertising, provided that all the purchasers in the offering are accredited investors.[4]

It is without doubt the responsibility of the Commission to implement Section 201 of the JOBS Act. It is equally without doubt that this responsibility cannot be separated from the Commission's duty to protect investors, maintain fair, orderly, and efficient markets, and facilitate capital formation. Congress established the Commission as the independent agency with the expertise and authority to administer the federal securities laws. By statute, the Commission has the power to make, amend, and rescind the rules and regulations needed from time to time to carry out the provisions of such laws.[5]

Nothing in the JOBS Act removes that broad authority. In fact, by tasking the Commission with implementing Section 201, Congress affirmed the Commission's responsibility for administering the Securities Act of 1933. Congress did not need to delegate this action to the SEC; it could have acted directly to exempt from registration any offering in which sales are made only to accredited investors.[6] But Congress declined to bypass the SEC. To the contrary, Section 201 expressly defers to the Commission's rulemaking authority.[7] The inescapable conclusion is that Congress intended the SEC, as a bipartisan Commission with broad rulemaking authority, to use its expertise to accomplish the goals of Section 201 in a manner consistent with the purpose of the Securities Act.

It is a false proposition to suggest that the Commission's hands are tied — and

that the JOBS Act prevents the Commission from protecting investors and safeguarding the integrity of the securities markets at the same time that it makes the changes required to Rule 506.[8]

The need for the Commission to exercise its authority and protect investors is great, because general solicitation clearly has the potential to put investors at risk. In short, without additional protections, general solicitation makes fraud easier and enforcement more difficult.

Without Additional Protections, Permitting General Solicitation Will Put Investors at Risk

The record is clear that general solicitation will make fraud easier by allowing fraudsters to cast a wider net for victims. The potential risks associated with general solicitation are well understood. Many experienced observers, including law professors, state securities regulators, and investor advocacy groups, have submitted extensive comment letters documenting their concerns.[9]

The Commission's own actions today recognize those risks.[10] Today's accompanying release proposing ways to mitigate the damage of general solicitation is a testament to that increased risk. However, while I welcome efforts to protect investors, any benefits from such proposals will come far too late for the investors who are harmed.

Proponents of the current process say that we shouldn't worry so much about fraud, because sales under Rule 506(c) are limited to accredited investors.[11] The theory is that accredited investors are presumed to be knowledgeable about financial matters and otherwise able to fend for themselves.[12] However, that argument is flawed in important ways:

First, the definition of accredited investor is not limited to experienced or sophisticated investors. An individual with annual income of $200,000 or net worth of $1,000,000[13] may be considered well-off, but those benchmarks are not necessarily correlated with financial expertise.[14] In fact, the SEC's Division of Economic and Risk Analysis estimates that only a small percentage of U.S. households meeting the definition of accredited investor have substantial direct holdings of individual securities, suggesting that their experience investing in securities may be limited.[15]

Second, general solicitation provides fraudsters with key advantages over legitimate capital raisers: For one thing, the scam artist does not feel compelled to tell the truth — but can make the sales pitch as compelling as imagination permits. For another, unlike real investment funds and companies raising money for a legitimate purpose, the Ponzi-schemer only cares about raking in as much money as possible, and has an unlimited number of shares to sell. Thus, without common sense protections, general solicitation will prove be a great boon to the fraudster. Experience tells us that this will lead to economic disaster for many investors. In addition, a market tainted by accounts of fraud will also be damaging for legitimate companies seeking to raise capital under Rule 506(c).[16]

The rulemaking record is replete with evidence raising these concerns. In fact, the Dodd-Frank mandated Investor Advisory Committee recognized these risks and acted unanimously last October to adopt a series of recommendations on general solicitation seeking to balance investor protection, capital formation, and market integrity.[17] In so doing, the Committee urged the Commission to "carefully consider the potential harm to investors … and the alternatives available to

minimize that harm."[18]

It is simply wrong for the Commission to brush these concerns aside and neglect its statutory responsibility to prevent fraud in the sale of securities sold in interstate commerce.

It is Reckless to Rush Forward with Adopting Rule 506(c), in the Hope that Investor Protections will be Added Later, Rather than Reproposing Now

Today, in addition to allowing general solicitation in Rule 506 offerings, the Commission is also considering a proposal to amend Regulation D and related rules to ameliorate the risks of general solicitation.[19] While I support that proposal, I strongly question the timing of the Commission's actions. The Commission is going ahead with the ***adoption*** of Rule 506(c), but only ***proposing*** the changes that would help to mitigate the harm to investors. The measures discussed in the accompanying proposal should have been considered as part of the amendments to allow general solicitation. I'm afraid the protections will simply come too late, if they come at all, for many investors.[20] It is reckless to create a known risk today, with just the hope of a speculative remedy tomorrow.

Let me use a transportation-related analogy to help put this into perspective:

Imagine that a new locomotive would allow trains to go much faster. I believe that a responsible way to proceed would be to examine the railroad tracks to see if they could handle that faster speed. We would probably find a lot of places where trains could safely go much faster. But there would also be curves and grade crossings where the faster speed would be dangerous, and we would need to adopt safeguards to help prevent accidents. Of course, some of us might differ about how to implement such precautions, but all of us would want to make sure that the railroads were safe at the new speeds, ***before*** they started hurtling through our towns.

By the same principle, lifting the ban on general solicitation can and should be done in a manner that ***concurrently*** promotes investor protection, and provides regulators with the tools they need to police the market effectively. Adopting Rule 506(c) today, while relying on speculative future actions to implement the common sense improvements needed to protect investors, is no way to run a railroad.

I hope that the Regulation D enhancements we propose today — together with needed improvements to the definition of accredited investor — will be adopted promptly, but experience tells me I shouldn't hold my breath. The Commission has proposed many rules that linger indefinitely without going into effect.[21]

The Rulemaking Process Was Fatally Flawed

So, how did we get here? Unfortunately, I believe the Commission's process for this rulemaking was fatally flawed from the beginning.

The primary error was the Commission's failure to even consider any alternatives when the removal of general solicitation was proposed. [22] It is standard practice in Commission rulemakings for the proposing release to request comment on both the terms of the rule proposed and any alternatives to the proposed rule. In fact, I cannot recall any substantive rulemaking during my terms as a Commissioner — and certainly no rulemaking as significant as this one — in which the release did not expressly solicit comments on potential alternatives.

But in this case all such requests for comment were pointedly excluded.[23] That

was a slap in the face to investors. More importantly, since the proposing release excluded any substantive discussion of the various suggestions to mitigate risk from general solicitation that were raised by commenters prior to the issuance of the proposal, the Commission was prevented from considering such suggestions at the adopting phase of the rulemaking. That is why I have consistently called for reproposal of the rule.

Numerous alternatives to the stripped-down version of the rule adopted here today are in the record, but — instead of considering them as part of the process of removing the ban on general solicitation, when it mattered most — the majority dismissed them out-of-hand, without data, without analysis, and without any substantive explanation.

This is bad policy for a regulatory agency. The Commission has a responsibility to fulfill its statutory duty to protect investors, maintain fair, orderly, and efficient markets, and facilitate capital formation — and, as one court has noted, it must do so "on the basis of empirical data and sound analysis."[24] By law, such analysis must include adequate consideration of reasonable alternatives.[25]

Identification of alternative regulatory approaches, together with an evaluation of the benefits and costs, both quantitative and qualitative, of the main alternatives, is also required by the guidance on economic analysis recently published by the SEC's staff.[26] Yet, this too was ignored.

The Commission's failure to adequately consider any alternatives to the version of the rule adopted, and to evaluate the effect of such alternatives on investor protection, including the costs to investors and other market participants of any increase in fraud resulting from general solicitation, is a fatal flaw in the rule that the majority of the Commission votes to adopt today.

The Commission also failed to adequately assess the economic effects of the new rule. The economic analysis in the adopting release includes numerous unsupported conclusions,[27] and unexplained contradictions,[28] and fails to respond to substantial problems raised by commenters.[29] Moreover, the adopting release acknowledges repeatedly that the Commission's data on the Rule 506 market is unreliable or incomplete, but then dismisses the impact of this lack on the Commission's economic analysis, without explanation.[30]

These failures cry out for reproposing a balanced rule that implements Section 201(a) in a manner consistent with the Commission's other statutory responsibilities. Failure to do so risks delay, uncertainty, and damage to the Commission's important mission by insisting on the adoption of an unbalanced and deficient rule.

For all these reasons, I cannot support this rule.

Lastly, I appreciate that, after a lengthy delay, the Commission is finally acting to fulfill its obligation under the Dodd-Frank Act to prevent felons and other "bad actors" from being involved in Rule 506 offerings. However, the Bad Actor rule is not a panacea that will solve the problems created today. For example, a Bad Actor rule can do nothing to protect investors from fraudsters who have yet to be caught and identified.[31]

Conclusion

Obviously, I am disappointed and saddened by the reckless adoption of the amendments to Rule 506 without appropriate safeguards. I know that many on

the staff share my concerns. I want to encourage you to fight on behalf of investors. They will need you now more than ever.

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[1] Today, the Commission is being asked to consider and vote on three actions: (i) the adoption of rule amendments to implement Section 201 of the JOBS Act, to remove the prohibition on general solicitation in certain exempt offerings, *Eliminating the Prohibition Against General Solicitation and General Advertising in Rule 506 and Rule 144A Offerings,* Release No. 33-[XXXX] (July 10, 2013) (the "*Adopting Release*"); (ii) the adoption of rule amendments to implement Section 926 of the Dodd-Frank Act, to disqualify certain felons and other "bad actors" from offerings pursuant to Rule 506, *Disqualification of Felons and Other "Bad Actors" from Rule 506 Offerings,* Release No. 33-[XXXX] (July 10, 2013) (the "*Bad Actor Adopting Release*"); and (iii) the proposal of rule and form amendments to enhance the Commission's ability to evaluate the development of market practices in Rule 506 offerings and address concerns that may arise in connection with permitting issuers to engage in general solicitation and general advertising under Rule 506(c), as amended today, *Amendments to Regulation D, Form D and Rule 156 under the Securities Act,* Release No. 33-XXXX (July 10, 2013) (the "*Reg D Proposing Release*").

[2] The rulemaking before us also implements Section 201(a)(2) of the JOBS Act, which requires the Commission to revise Rule 144A under the Securities Act of 1933 (the "Securities Act") to provide that securities sold under that exemption may be offered to persons other than qualified institutional buyers, including by means of general solicitation or advertising, provided that the securities are sold only to persons reasonably believed to be qualified institutional buyers. Because of the nature of the 144A market, this change does not present the same risks to individual investors as the proposed amendment to permit general solicitation under Rule 506(c) of Regulation D.

[3] Jumpstart Our Business Startups Act, §103, Pub. L. No. 112-106, 126 Stat. 306 (April 5, 2012).

[4] Currently, Rule 506 is a non-exclusive safe harbor under Section 4(a)(2) (formerly Section 4(2)) of the Securities Act, which exempts transactions by an issuer "not involving any public offering" from the registration requirements of Section 5 of the Securities Act. Under existing Rule 506, an issuer may sell securities, without any limitation on the offering amount, to an unlimited number of "accredited investors," as defined in Rule 501(a) of Regulation D, and to no more than 35 non-accredited investors who meet certain "sophistication" requirements, provided that neither the issuer, nor any other person acting on its behalf, shall offer or sell the securities by any form of general solicitation or general advertising. Certain information requirements apply to sales to non-accredited investors, but if sales are made only to accredited investors, no disclosure requirements are mandated, although antifraud rules continue to apply. As contemplated by the rule amendments considered today, that exemption will remain in place as Rule 506(b), and a new exemption will be promulgated as Rule 506(c), which permits general solicitation and advertising so long as sales are not made to non-accredited investors and the issuer takes reasonable steps to verify that all purchasers are accredited. Securities acquired in a transaction under Rule 506 (whether or not general solicitation is used) are so-called "restricted securities" that cannot be resold without registration under the Securities Act or an exemption therefrom. It is a condition to any offering under Rule 506 that the issuer exercise reasonable care to assure that the purchasers of the securities are not "underwriters" as defined under the Act.

[5] *See, e.g.,* Securities Act of 1933 §19(a); Securities Exchange Act of 1933 §23(a).

[6] In fact, Congress considered, and declined to enact, a bill that would have amended the Securities Act to expressly permit general solicitation. *See*, Access to Capital for Job Creators, H.R. 2940 and S. 1831, 112th Cong. (2011). Such bills would have amended Section 4 of the Securities Act to exempt transactions not involving any public offering "whether or not such transactions involve general solicitation or general advertising." By contrast, Section 201(b) of the JOBS Act amends Section 4 of the Securities Act to permit general solicitation and general advertising *only* in offers and sales exempted from registration by the Commission under Rule 506 of Regulation D. *See also*, letter to the Commission from Senators Jack Reed, Carl Levin, Dick Durbin, Tom Harkin, Frank R. Lautenberg, Al Franken, and Daniel K. Akaka, U.S. Senate (Oct. 12, 2012) ("Congress could have removed from the Commission any authority to condition, limit, or otherwise regulate the manner or substance of general solicitation. Instead, Congress clearly elected to allow the Commission to retain its authority to regulate this new allowance for general solicitation in offerings exempt from registration pursuant to Rule 506 or Rule 144A.")

[7] Section 201(a)(1) does not prohibit all regulation of general solicitation and advertising, it only addresses the particular prohibition currently contained in Rule 502(c) of Regulation D, requiring that *such prohibition* shall not apply to offers and sales pursuant to Rule 506, if all purchasers are accredited investors.

[8] *See, Eliminating the Prohibition Against General Solicitation and General Advertising in Rule 506 and Rule 144A Offerings*, Release No. 33-9354 (Aug. 29, 2012) [77 FR 54464], *available at* http://www.sec.gov/rules/proposed/2012/33-9354.pdf ("Proposing Release"), at p. 9 ("In this release, we are proposing only those rule and form amendments that are, in our view, necessary to implement the mandate in Section 201(a).")

[9] *See, e.g.,* letters from North American Securities Administrators Association ("NASAA") (Oct. 3, 2012); Consumer Federation of America ("Consumer Federation") (Oct. 3, 2012); Consumer Federation, Americans for Financial Reform, and AFL-CIO (Apr. 23, 2013); AARP (Oct. 5, 2012); Fund Democracy, Inc. ("Fund Democracy") (Oct. 2, 2012); Massachusetts Securities Division (Sept. 20, 2012); Nevada Securities Division (Oct. 5, 2012); Ohio Division of Securities (Oct. 5, 2012); South Carolina Securities Commissioner (Oct. 5, 2012); Virginia Division of Securities (Oct. 4, 2012); Investment Company Institute (Oct. 5, 2012), BetterInvesting (Oct. 19, 2012); CFA Institute (Nov. 1, 2012); and Christopher Hunter, Ph.D., Prof. of Sociology, Grinnell College (Sept. 1, 2012) (each in Comments on Proposed Rule: Eliminating the Prohibition Against General Solicitation and General Advertising in Rule 506 and Rule 144A Offerings ("File No. S7-07-12"), *available at* http://www.sec.gov/comments/s7-07-12/s70712.shtml); and letter from Prof. Mercer Bullard, President and Founder, Fund Democracy, Prof. J. Robert Brown, Jr., Director, Corporate & Commercial Law Program, University of Denver Sturm College of Law, and Barbara Roper, Consumer Federation (Aug. 28, 2012) in Comments on SEC Regulatory Initiatives Under the JOBS Act: Title II — Access to Capital for Job Creators (the "*Pre-Proposal File*"), *available at* http://www.sec.gov/comments/jobs-title-ii/jobs-title-ii.shtml.

[10] The Commission is well aware of the concerns regarding general solicitation. *See*, Adopting Release, 11("We acknowledge the concerns of some commenters that the elimination of the prohibition against general solicitation for a subset of Rule 506 offerings may affect the behavior of issuers and other market

participants in ways they believe could compromise investor protection.") In fact, the release expressly acknowledges that "[e]liminating the prohibition against general solicitation could result in heightened fraudulent activity in Rule 506(c) offerings because it will be easier for promoters of fraudulent schemes to reach potential investors through general solicitation." *Id.,* 91.

[11] *See, e.g.,* letter from BlackRock (Oct. 5, 2012) in File No. S7-07-12; and letter from National Small Business Association (Jun 12, 2012) in Pre-Proposal Comment File.

[12] *Proposed Revision of Certain Exemptions from the Registration Provisions of the Securities Act of 1933 for*

Transactions Involving Limited Offers and Sales, Release No. 33-6339, 46 FR 41791, 41802 (Aug. 7, 1981) ("This approach is based on the presumption that accredited investors can fend for themselves without the protections afforded by registration….").

[13] The definition of "accredited investor" applicable to Rule 506 is set forth in Rule 501(a) of Regulation D [17 CFR 230.501(a)] and includes any person who comes within one of the definition's enumerated categories of persons, or whom the issuer "reasonably believes" comes within any of the enumerated categories, at the time of the sale of the securities to that person. The categories include (A) any natural person whose individual net worth, or joint net worth with that person's spouse, exceeds $1,000,000, excluding the person's primary residence and any indebtedness secured thereby (up to the value of such residence), and (B) any natural person who had an individual income in excess of $200,000 in each of the two most recent years or joint income with that person's spouse in excess of $300,000 in each of those years and has a reasonable expectation of reaching the same income level in the current year.

[14] For example — and without limiting my broad concerns over the accredited investor definition — many households meeting the accredited investor threshold are likely to be elderly, with savings accumulated over the course of decades (which must, in turn, last the rest of a lifetime). I am particularly concerned that seniors may be targeted by general solicitations, as many older Americans may lack the financial literacy necessary to understand the risks of an investment in restricted, unregistered securities. *See*, Staff Study Regarding Financial Literacy Among Investors As Required by Section 917 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Aug. 2012), *available at* http://www.sec.gov/news/studies/2012/917-financial-literacy-study-part1.pdf, p. 15 ("…surveys demonstrate that certain subgroups, including women, African-Americans, Hispanics, the oldest segment of the elderly population, and those who are poorly educated, have an even greater lack of investment knowledge than the average general population.") This risk may be heightened by a regulatory regime that permits cold-calling and other forms of general solicitation. I am concerned that seniors and other unsophisticated investors targeted for their relative wealth will not be protected by the definition of "accredited investor," but in fact made more vulnerable because of it.

[15] *See,* Adopting Release at pp. 77-78.

[16] These concerns are heightened by the fact that general solicitation may actually make it harder for state securities commissions and other law enforcement agencies to enforce the federal securities laws. Currently, since general solicitation is prohibited in Rule 506 offerings, such activities are a red flag to both investors and regulators alike. When Rule 506(c) becomes effective, such

early-warning benefits will be lost, as the limited conditions to Rule 506(c) can only be tested when the transaction closes. Moreover, since it is easier to establish a violation of the registration and prospectus requirements of the Securities Act than it is to prove fraud, scams that rely on general solicitation can now often be shut down relatively quickly. Rule 506(c) would make it almost impossible to do so before the damage has been done and the money lost.

[17] The Investor Advisory Committee was established by Section 911 of the Dodd-Frank Act to advise the Commission on regulatory priorities, the regulation of securities products, trading strategies, fee structures, the effectiveness of disclosure, and on initiatives to protect investor interests and to promote investor confidence and the integrity of the securities marketplace. The Committee is comprised of individuals with diverse expertise representing a wide variety of investor interests and is authorized to submit findings and recommendations for review and consideration by the Commission. The Commission has a statutory duty to review the findings and recommendations of the Investor Advisory Committee and, each time the Committee submits a finding or recommendation to the Commission, to promptly issue a public statement assessing the finding or recommendation of the Committee and disclosing the action, if any, the Commission intends to take with respect to the finding or recommendation. *See*, Section 39(g) of the Securities Exchange Act of 1934. Sadly, the Commission has neglected this responsibility, further impairing the rulemaking process.

[18] Recommendations of the Investor Advisory Committee Regarding SEC Rulemaking to Lift the Ban on General Solicitation and Advertising in Rule 506 Offerings: Efficiently Balancing Investor Protection, Capital Formation and Market Integrity, at p. 1 (Oct. 12, 2012), *available at* http://www.sec.gov/spotlight/investor-advisory-committee-2012/iac-general-solicitation-advertising-recommendations.pdf.

[19] Reg D Proposing Release. *See,* Luis A. Aguilar, Statement at SEC Open Meeting (July 10, 2013).

[20] Other actions referred to in the proposing release are even more speculative. The release states that Commission staff has developed a work plan to monitor, review and analyze the use of Rule 506(c), including monitoring the Rule 506(c) market for indications of fraud. While I welcome any effort by the Commission to better inform our rulemaking and enforcement efforts, I am struck by the fact that the need for such a work plan is simply further confirmation that the majority's rule fails to address the risks to investors inherently posed by general solicitation.

[21] *See, e.g., Amendments to Regulation M: Anti-Manipulation Rules Concerning Securities Offerings,* Release No. 33-9511 (Dec. 9, 2004); *Investment Company Governance,* Release No. IC-26323 (Jan. 15, 2004); *Regulation of Non-Public Trading Interest [i.e., "Dark Pools"],* Release No. 34-60997 (Nov. 13, 2009). *See, also, Political Contributions by Certain Investment Advisers [i.e., "Pay-to-Play"],* Release No. IA-3043 (July 1, 2010), which was first proposed by the Commission more than a decade before its eventual adoption. Release No. IA-1812 (Nov. 1, 1999).

[22] Shortly after the JOBS Act became law, the Commission invited the public to make its views known on various initiatives under the Act, by submitting comment letters to the Commission's website. Over 60 comment letters were received prior to the open meeting vote on the general solicitation proposal. Other commenters came to the Commission to meet with Commissioners and staff in person. As the Commission has acknowledged, many of the pre-proposal commenters urged the

Commission to consider and propose rule and form amendments in connection with the implementation of JOBS Act Section 201. However, the proposing release failed to consider any of the recommendations made by commenters to mitigate the risks of general solicitation.

[23] *See,* Proposing Release 9-10 ("… we are requesting comment on various issues relating specifically to the proposed amendments described above. In this release, we are proposing only those rule and form amendments that are, in our view, necessary to implement the mandate in Section 201(a). We recognize that commentators have urged us to consider and propose other amendments to Regulation D or to Form D that they believe are appropriate in connection with implementation of the rule and form amendments proposed here. *** We appreciate the suggestions made by these commentators; however, at this time, we are not proposing these or any other amendments to Regulation D or to Form D.")

[24] *Business Roundtable v. Securities and Exchange Com'n*, 647 F.3d 1144, 1148 (C.A.D.C., 2011) (quoting Commissioner Kathleen L. Casey).

[25] *Chamber of Commerce of U.S. v. Securities and Exchange Com'n*, 412 F.3d 133, 144-45 (C.A.D.C., 2005).

[26] Memorandum dated March 16, 2012, from the SEC's Division of Risk, Strategy and Financial Innovation (now known as the Division of Economic and Risk Analysis) and the SEC's Office of the General Counsel, to the staff of the SEC's rulewriting divisions and offices, re: Current Guidance on Economic Analysis in SEC Rulemakings, at pp. 9-10, *available at* http://www.sec.gov/divisions/riskfin/rsfi_guidance_econ_analy_secrulemaking.pdf. Reasonable alternatives include only those that are available to the SEC and accordingly would not include provisions that the SEC lacks the authority to implement, or that would not effectively address the need sought to be addressed by the proposed rulemaking. However, as discussed above, the Commission has authority to regulate offerings pursuant to Rule 506 in accordance with the federal securities laws, including offerings using general solicitation, and Congress did nothing to reduce or rescind such authority.

[27] For example, the adopting release states that "[t]he risks to investors of fraudulent offerings conducted under Rule 506(c) may be mitigated to some extent by the requirement that issuers sell only to accredited investors (and take reasonable steps to verify such status), who***, by virtue of meeting the requirements of the definition,*** may be better able to assess their ability to take financial risks and bear the risk of loss than investors who are not accredited." Adopting Release, pp. 95 (emphasis added). However, no data is offered whatsoever to support the conclusion that accredited investors "may be better able to assess their ability to take financial risks."

[28] The adopting release also states that "only a small percentage" of households that qualify as accredited investors "are likely to participate in securities offerings, especially exempt offerings." Adopting Release, p. 77. However, in assessing the benefits of the rule, the release also states that, "As a result [of general solicitation], we anticipate that issuers will be able to reach a much greater number of potential investors than is currently the case…." *Id.,* 83. No attempt is made to explain this contradiction.

[29] For example, the adopting release states as a potential benefit of the rule that lower issuance costs could improve the efficiency of capital flow, if issuers use Rule 506(c) in lieu of registered offerings. Adopting Release, p. 83. However, the

release fails to address how substituting Rule 506(c) for registered offerings may affect allocative or informational efficiency, as investment decisions are made without the benefit of the disclosures required in a registration statement and prospectus.

[30] Adopting Release, p. 65 ("… we believe that we do not have a complete view of the Rule 506 market, particularly with respect to the amount of capital raised."), p. 73 ("We have relatively little information on the types and numbers of investors in Rule 506 offerings."), p.76 ("… we do not know what percentage of investors in Rule 506 offerings are natural persons…."), p. 88 ("… there are significant data and informational limitations on our ability to quantify the economic impact of eliminating [the prohibition against general solicitation]"). The release goes on to cite the Commission's experience with Rule 504 in the period from 1992 to 1999 as support (*see*, Adopting Release, p. 85) for the otherwise completely speculative conclusion that "allowing issuers to have wider access to accredited investors by eliminating the prohibition against general solicitation … will significantly improve their access to capital and potentially enhance capital formation and lower the issuance cost." (*Id.,* 83-84) — even though in two other places the release states that the Rule 504 general solicitation experience was not comparable. *Id.,* 82 ("… we believe that there are sufficient differences between Rule 504, as amended to permit general solicitation from 1992 to 1999, and Rule 506(c) such that it would not be useful to look to the Rule 504 market during that period to make meaningful predictions as to the type or magnitude of the effects of eliminating the prohibition against general solicitation for Rule 506(c) offerings"), and *Id.,* 93 ("We do not believe that our experience with offerings conducted pursuant to Rule 504, as amended in 1992, is particularly instructive with respect to the potential incidence of fraud resulting from our implementation of Section 201(a) of the JOBS Act…."). The release also fails to indicate whether the increase in Rule 504 offerings over the late 1990s represented additional capital raising or the substitution of one form of capital raising for another.)

[31] An even greater concern in the Bad Actor rule as adopted is that "bad actors" are not disqualified unless the felony conviction, injunction, or order that would trigger disqualification occurs after the rule's effective date. I do not believe that Congress intended to limit bad actor disqualification to such extent. It is particularly disappointing that the Commission allowed this rule to languish for more than two years, while numerous "bad actors" received court sanctions that could have — but now will not — disqualify them from taking advantage of Rule 506 for years to come. Bad Actor Adopting Release. *See,* Luis A. Aguilar, "Limiting — But Not Eliminating — Bad Actors from Certain Offerings," Statement at SEC Open Meeting (July 10, 2013).

http://www.sec.gov/news/speech/2013/spch071013laa.htm
