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August 8, 2013

The Honorable Tim Johnson
Chairman
The Honorable Michael D. Crapo
Ranking Member
Committee on Banking, Housing, and Urban Affairs
United States Senate

The Honorable Jeb Hensarling
Chairman
The Honorable Maxine Waters
Ranking Member
Committee on Financial Services
House of Representatives

Subject: Securities and Exchange Commission: Eliminating the Prohibition Against General Solicitation and General Advertising in Rule 506 and Rule 144A Offerings

Pursuant to section 801(a)(2)(A) of title 5, United States Code, this is our report on a major rule promulgated by the Securities and Exchange Commission (Commission) entitled "Eliminating the Prohibition Against General Solicitation and General Advertising in Rule 506 and Rule 144A Offerings" (RIN: 3235-AL34). We received the rule on July 11, 2013. It was published in the *Federal Register* as final rules on July 24, 2013, with an effective date of September 23, 2013. 78 Fed. Reg. 44,771.

The final rule implements section 201(a) of the Jumpstart Our Business Startups Act (JOBS Act)¹ by amending the Commission's Rule 506 of Regulation D and Rule 144A under the Securities Act of 1933. The amendment to Rule 506 permits an issuer to engage in general solicitation or general advertising in offering and selling securities pursuant to Rule 506, provided that all purchasers of the securities are accredited investors and the issuer takes reasonable steps to verify that such purchasers are accredited investors. The amendment to Rule 506 also includes a non-exclusive list of methods that issuers may use to satisfy the verification requirement for purchasers who are natural persons. The amendment to Rule 144A provides that securities may be offered pursuant to Rule 144A to persons other than qualified institutional buyers, provided that the securities are sold only to persons that the seller and any person acting on behalf of the seller reasonably believe are qualified institutional buyers. The Commission is also revising Form D to require issuers to indicate whether they are relying on the provision that permits general solicitation or general advertising in a Rule 506 offering.

¹ Pub. L. No. 112-106, § 201(a), 126 Stat. 306, 313-314 (2012).

Enclosed is our assessment of the Commission's compliance with the procedural steps required by section 801(a)(1)(B)(i) through (iv) of title 5 with respect to the rule. Our review of the procedural steps taken indicates that the Commission complied with the applicable requirements.

If you have any questions about this report or wish to contact GAO officials responsible for the evaluation work relating to the subject matter of the rule, please contact Shirley A. Jones, Assistant General Counsel, at (202) 512-8156.

signed

Robert J. Cramer
Managing Associate General Counsel

Enclosure

cc: Elizabeth M. Murphy
Secretary
Securities and Exchange Commission

REPORT UNDER 5 U.S.C. § 801(a)(2)(A) ON A MAJOR RULE
ISSUED BY THE
SECURITIES AND EXCHANGE COMMISSION
ENTITLED
"ELIMINATING THE PROHIBITION AGAINST
GENERAL SOLICITATION AND GENERAL ADVERTISING
IN RULE 506 AND RULE 144A OFFERINGS"
(RIN: 3235-AL34)

(i) Cost-benefit analysis

The Securities and Exchange Commission (Commission) discussed the costs and benefits of this final rule. The Commission noted that some of the costs and benefits stem from the statutory mandate while others are affected by the discretion the Commission exercised in implementing this mandate and that these two types of costs and benefits may not be entirely separable. The Commission also noted that because Rule 506 has always been subject to the prohibition against general solicitation, there are significant data and informational limitations on its ability to quantify the economic impact of eliminating that prohibition in certain Rule 506 offerings.

The Commission described certain benefits it expects this final rule to have for issuers. The Commission found that the elimination of the prohibition against general solicitation for a subset of Rule 506 offerings will enable issuers to solicit potential investors directly, through both physical (such as mailings, newspaper advertisements, and billboards) and electronic (such as the Internet, social media, email, and television) means. As a result, the Commission anticipates that issuers will be able to reach a much greater number of potential investors than is currently the case, thereby increasing their access to sources of capital. The Commission believes that it is reasonable to conclude that allowing issuers to have wider access to accredited investors by eliminating the prohibition against general solicitation for a category of Rule 506 offerings will significantly improve their access to capital and potentially enhance capital formation and lower the issuance cost. The Commission also found that the elimination of the prohibition against general solicitation would also reduce the uncertainty for issuers as to whether Rule 506 offerings can be completed in certain situations and would eliminate the costs of complying with the prohibition.

The Commission also described certain benefits it expects this final rule to have for investors. It found that the elimination of the prohibition against general solicitation in Rule 506(c) offerings will likely increase the amount and types of information about issuers and offerings that are communicated to investors, which could also lead to more efficient pricing for the offered securities. In addition, accredited investors who previously have found it difficult to find investment opportunities in Rule 506 offerings may be able to find and potentially invest in a larger and more diverse pool of potential investment opportunities, which would result in a more efficient allocation of investments by accredited investors. Thus, Rule 506(c) could increase capital formation and at the same time improve the efficiency of its allocation.

The Commission also discussed the costs of this final rule. The Commission found that eliminating 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. An increase in fraud would not only harm those investors who are defrauded, but it would undermine investor participation in Rule 506(c) offerings and could negatively affect capital-raising by legitimate issuers—for example, by reducing investor participation in Rule 506(c) offerings—thereby inhibiting capital formation and reducing efficiency. In addition, some issuers with publicly-traded securities may use general solicitation for a purported Rule 506(c) offering to generate investor interest in the secondary trading markets, especially in the over-the-counter markets, which could be used by insiders to resell securities at inflated prices. This would impose costs to investors in these secondary markets, as well as investors in Rule 506(c) offerings, and could erode investor participation in Rule 506(c) offerings, thus potentially raising the cost of capital for issuers in this market.

(ii) Agency actions relevant to the Regulatory Flexibility Act (RFA), 5 U.S.C. §§ 603-605, 607, and 609

The Commission prepared a Final Regulatory Flexibility Analysis for this final rule. The analysis discussed the reasons for, and objectives of the rulemaking; significant issues raised by the public; small entities subject to the final rule and form amendments; projected reporting, recordkeeping, and other compliance requirements; duplicative overlapping or conflicting federal rules; and significant alternatives.

(iii) Agency actions relevant to sections 202-205 of the Unfunded Mandates Reform Act of 1995, 2 U.S.C. §§ 1532-1535

As an independent regulatory agency, the Commission is not subject to the Act.

(iv) Other relevant information or requirements under acts and executive orders

Administrative Procedure Act, 5 U.S.C. §§ 551 et seq.

On August 29, 2012, the Commission published a proposed rule. 77 Fed. Reg. 54,464. The comment period for the proposed rule and form amendments closed on October 5, 2012. The Commission received over 225 comment letters on the proposing rule, including from professional and trade associations, investor organizations, law firms, investment companies and investment advisers, Members of Congress, the Commission's Investor Advisory Committee, state securities regulators, issuers, individuals, and other interested parties. The Commission responded to public comments in the final rule.

Paperwork Reduction Act (PRA), 44 U.S.C. §§ 3501-3520

The Commission determined that this final rule contains an information collection requirement under the Act. The Commission has submitted the requirement to the Office of Management and Budget (OMB) for review. The title of the requirement is "Form D," and it has OMB Control Number 3235-0076. The Commission estimates that under this rule the requirement will have 21,824 responses with 4 burden hours each for a total burden of 87,296 hours and a total cost of \$26,188,800.

Statutory authorization for the rule

The Commission promulgated this final rule under the authority of sections 4(a)(1), 4(a)(2), 7, 17(a), 19, and 28 of the Securities Act of 1933, as amended, sections 2, 3, 9, 10, 11A(c), 12, 13, 14, 15(c), 15(g), 17(a), 23(a), and 30 of the Securities Exchange Act of 1934, as amended,

sections 23, 30, and 38 of the Investment Company Act of 1940, as amended, and section 201(a) of the JOBS Act. 15 U.S.C. §§ 77d(a)(1), 77d(a)(2), 77g, 77p, 77s, 77z-3, 78b, 78c, 78i, 78j, 78k-1(c), 78l, 78m, 78n, 78o(c), 78o(g), 78q(a), 78w(a), 78dd, 80a-23, 80a-29, 80a-37, 77d note.

Executive Order No. 12,866 (Regulatory Planning and Review)

As an independent regulatory agency, the Commission is not subject to the review requirements of this Order.