



## LEGAL ALERT

December 20, 2016

### **SEC Eases Rules Relating to Capital Raising**

On October 26, 2016, the SEC adopted final rules which will ease restrictions on certain types of offerings. The impact of these rule changes are discussed below and a chart for easy comparison of capital raising options under SEC Regulation D is attached for easy reference.

#### **New SEC Rule 147A for In-State Offerings**

Heretofore, the SEC exemption for in-state offerings required that all offers **and** sales be made to residents of one state by an issuer resident in, doing business in, and organized under the laws of, that state. In an age of electronic media, many issuers did not use this exemption for fear that an “offer” might get transmitted to a non-state resident thereby jeopardizing the availability of that exemption. Also, the exemption would not be available in circumstances where issuer had its principal place of business and a majority of its shareholders in Pennsylvania but was organized under Delaware law.

The SEC has addressed this concern by adopting new Rule 147A which provides an exemption for offerings made to residents of the state where the issuer has its principal place of business, is doing business and all sales are made to residents of that state. Therefore, even if an “offer” was transmitted by a Pennsylvania resident to his cousin in Maryland, the exemption would not be lost if all sales in such offering were made only to Pennsylvania residents. An issuer may comply with the “doing business in the state” requirement by meeting one of four different tests, including that a majority of its employees are based in the state.

Furthermore, there is no limitation as to the maximum amount of securities that may be offered in the state and there is no filing requirement with the SEC. Although there still remains a limitation on resale of securities sold under Rule 147A, the SEC has reduced the time from nine months after the date of last sale in the offering to six months after the date of sale of the security. SEC Rule 147A becomes effective on April 20, 2017.

While securities offered under the exemption contained in Rule 147A remain subject to the registration provisions of the Pennsylvania Securities Act of 1972, as amended (the “1972 Act”), Section 203(t) of the 1972 Act provides a state-level exemption (for which a filing is required) for offerings where all sales are made to Accredited Investors.

#### **Revised SEC Rule 504**

Previously, the exemption contained in Rule 504 of SEC Regulation D was limited to a maximum of \$1 million in a 12 month period. Effective January 20, 2017, this limitation has been increased to \$5 million.

The most obvious advantage to issuers using revised Rule 504 is the increase in the amount of securities which may be offered under that exemption.

The second advantage is that the prohibition on the use of general advertising and general solicitation and the six month limitation on resale normally applicable to a Rule 504 offering does not apply where the offering is made exclusively according to

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state law exemptions from registration that permit general solicitation and general advertising as long as sales are made only to Accredited Investors (e.g., Section 203(t) of the 1972 Act).

Where an issuer seeks to make an offering of \$5 million or less and is willing to limit sales only to Accredited Investors, an offering under revised Rule 504 may be worthy of examination as an alternative to a Rule 506(c) offering under SEC Regulation D.

The advantage of a Rule 506(c) offering is that, although a copy of SEC Form D must be filed with states where sales occur, states are preempted from review of these offerings. The disadvantage to a Rule 506(c) offering is that the issuer must “verify” that each purchaser is an Accredited Investor which imposes a higher standard of due diligence on the issuer than a Rule 506(b) or Rule 504 offering.

The advantage of a revised Rule 504 offering is that the issuer can use general solicitation and general advertising (in accordance with the provisions in the state Accredited Investor exemptions); there is no limitation on resales if resold to another Accredited Investor and there is no requirement to “verify” that the purchaser is an Accredited Investor even though the issuer must form a reasonable belief that each purchaser meets that standard. The disadvantage is that the issuer generally must make a notice filing and pay a filing fee in each state where a sale occurs.

### **Need More Information?**

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**COMPARISON OF CAPITAL RAISING OPTIONS UNDER SEC REGULATION D EXEMPTIONS  
REFLECTING CHANGES ADOPTED IN SEC RELEASE NO. 33-10238 (OCTOBER 26, 2016)**

<b>Applicable SEC Rule</b>	<b>Maximum Offering Amount</b>	<b>Type of Investors Allowed</b>	<b>“Bad Actor” Disqualification Provisions Apply</b>	<b>Restriction on Resale Applies</b>	<b>General Advertising/ General Solicitation Permitted</b>	<b>Form D Notice Filed with SEC</b>	<b>State Securities Law Compliance</b>	<b>Special Notes</b>
Rule 504	\$5 million (Eff. 1/20/17)	Any	Yes. (Eff. 1/20/17)	Yes, 6 months.	No.	Yes.	State Registration Required	Right of Withdrawal Notice
Rule 504(b)(iii)	\$5 million (Eff. 1/20/17)	Accredited Investors Only	Yes. (Eff. 1/20/17)	No, but state law requires resales to Accredited Investors only for first 12 months.	Yes.	Yes.	Pre-sale Filing under State Accredited Investor Exemptions (PA Form E)	Issuer must meet reasonable belief standard for Accredited Investors.
Rule 505	\$5 million	<del>Accredited Investors &amp; ≤ 35 non-Accredited Investors</del>	<del>Yes.</del>	<del>Yes.</del>	<del>No.</del>	<del>Yes.</del>	<del>Notice</del>	<b>Repealed (Eff. 5/22/17)</b>
Rule 506(b)	None.	Accredited Investors & ≤ 35 Qualified Investors	Yes. (Eff. 9/23/13)	Yes, 6 months.	No.	Yes.	Form D and filing fee in states where sales occur	Issuer must meet reasonable belief standard for Accredited Investors.
Rule 506(c)	None.	Accredited Investors Only	Yes. (Eff. 9/23/13)	Yes, 6 months.	Yes.	Yes.	Form D and filing fee in states where sales occur	Issuer must “verify” status as Accredited Investor.

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