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FRIED FRANK

June 1, 2020

VIA ELECTRONIC SUBMISSION

Vanessa A. Countryman
Secretary
U.S. Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549-1090

Re: Request for Comment Regarding SEC Release Nos. 33-10763 and 34-88321 (File Number S7-05-20): Facilitating Capital Formation and Expanding Investment Opportunities by Improving Access to Capital in Private Markets

Dear Secretary Countryman:

Fried, Frank, Harris, Shriver & Jacobson LLP ("**Fried Frank**") respectfully submits this letter in response to a request by the Securities and Exchange Commission (the "**Commission**") for comments regarding the above referenced release (the "**Proposing Release**").[1] We recognize the time and effort invested by the Commission and the staff of the Commission in formulating the Proposing Release, and appreciate the opportunity to provide comments regarding the release.

Fried Frank is an international law firm with offices in New York, Washington, D.C., London and Frankfurt. Our clients include many advisers to alternative investment funds, and we regularly counsel clients with respect to the formation and offering of interests in the investment funds that they advise. These comments, while informed by our experience in representing these clients, represent Fried Frank's own views and are not intended to reflect the views of our clients.

I. Introduction

We appreciate the Commission's efforts to simplify, harmonize and improve aspects of the exempt offering framework and believe that such efforts will reduce unnecessary uncertainty regarding the application of integration principles with respect to common fact patterns, thereby making it easier, and less costly, for issuers to access the capital markets while preserving investor protections.

Many of the comments we provide below recommend that the Commission take action that will reduce some of the uncertainty regarding the application of Rule 506(c). We believe this is

[1] Facilitating Capital Formation and Expanding Investment Opportunities by Improving Access to Capital in Private Markets, 85 Fed. Reg. 17956 (proposed Mar. 31, 2020) (to be codified at 17 C.F.R. pts. 227, 229, 230, 239, 249, 270 & 274).

appropriate in order to more fully realize the directive in Section 201(a)(1) of the Jumpstart Our Business Startups Act (the "**JOBS Act**")[2] that the Commission permit general solicitation or general advertising in offerings made under Rule 506, provided that all purchasers of the securities are accredited investors. Eight years after the JOBS Act became law, offerings relying on Rule 506(c) remain uncommon. The Commission's own estimates in this regard are striking. Table 1 of the Proposing Release estimates that in 2019, while issuers raised more capital in reliance on Rule 506 than on any other exemption, 96% of such capital was raised in reliance on Rule 506(b) and only 4% was raised in reliance on Rule 506(c).[3]

We believe that the enormous disparity between the amount of capital raised in reliance on Rule 506(b) versus the amount raised in reliance on Rule 506(c) is, to a great extent, due to the uncertainties involved in the application of the latter, certain of which relate to questions regarding the application of integration principles. We further believe that the opportunity to amend the rules relating to integration, as contemplated by the Proposing Release, creates the appropriate opportunity for the Commission to provide issuers with the guidance they need to actualize the intent of Section 201(a)(1) of the JOBS Act by enabling them to confidently raise capital via Rule 506 offerings that use general solicitation,[4] so long as all purchasers in such offerings are accredited investors.

Set forth below are our comments, which we respectfully submit with respect to the Proposing Release:

A. Integration.

(1) The Commission should revise proposed Rule 152(a)(1) to clarify that, so long as its conditions are satisfied, an issuer may concurrently engage in an offering in reliance on Rule 506(b) and another offering in reliance on Rule 506(c), even if the investors who purchase securities in the Rule 506(c) offering were solicited using general solicitation.

(2) The Commission should revise proposed Rule 152(b)(1) to provide that when an exempt offering for which general solicitation is not permitted is made more than 30 days after the termination of another offering, the two offerings will not be integrated, regardless of whether the purchasers in the exempt offering not permitting general solicitation may have been solicited using general solicitation or had established a substantive relationship with the issuer prior to the commencement of the offering.

(3) The Commission should include an additional safe harbor in proposed Rule 152(b) providing that any offering commenced in reliance on an exemption that does not permit general solicitation can be continued in reliance on an exemption that does permit general solicitation. If the Commission declines to include that new safe

[2] Pub. L. No 112-106, Section 201(a), 126 Stat. 306, 313 (April 5, 2012).
[3] Proposing Release at 17958.
[4] All references in this letter to "general solicitation" also refer to "general advertising."

harbor, we believe it should clarify that an issuer can accomplish the same result pursuant to the safe harbor in proposed Rule 152(b)(4).

(4) The Commission should revise proposed Rule 152(c)(ii) to clarify that an issuer can seamlessly terminate an offering in reliance on one exemption and simultaneously commence an offering of those securities in reliance on another offering exemption. In addition, the Commission should state that it is not necessary for an issuer to use different offering materials for offerings that rely on different exemptions.

(5) The Commission should clarify that, consistent with the principle behind proposed Rule 152(a)(1), general solicitations by the issuer in connection with a primary offering in reliance on Rule 506(c) or another offering that permits general solicitation will not be integrated with an investor's secondary offering in reliance on Section 4(a)(7), so long as (i) the investors in the offering in reliance on Section 4(a)(7) were not solicited through the use of general solicitation or (ii) the purchasers established a substantive relationship with the issuer or the investor (or a person acting on behalf of the issuer or the investor) prior to the commencement of the offering in reliance on Section 4(a)(7).

(6) The Commission should not enact proposed Rule 906. We recommend that the Commission address the uncertainty among market participants regarding whether it is possible to conduct concurrent Regulation S and Rule 506(c) offerings by revising Rule 902 to expressly provide that the prohibition on "directed selling efforts" is not applicable when the Regulation S offering is made concurrently with an offering (a) in reliance on an exemption that permits general solicitation, so long as the issuer does not engage in such general solicitation for the purpose of conditioning the market in the United States for any securities being offered in reliance on Regulation S or (b) registered under the Securities Act of 1933, as amended (the "**Securities Act**").[5] We also recommend that the Commission clarify that the issuer is not required to provide evidence for its intent. In addition, we recommend that the Commission state that concurrent Rule 506(c) and Regulation S offerings will not be integrated even if the issuer uses the same (or substantially identical) offering materials for the offerings.

(7) The Commission should amend Rule 502(c) to provide that a general solicitation shall be deemed to not have occurred with respect to an offering for which general solicitation is prohibited if all of the purchasers in such offering (i) were not solicited through the use of general solicitation or (ii) established a substantive relationship with the issuer (or a person acting on the issuer's behalf) prior to the commencement of the offering.

B. Substantive pre-existing relationships.

[5] 15 U.S.C. §77a *et seq.*

(1) The Commission should state that a broker-dealer or investment adviser may offer interests in private funds that rely on the exclusions from the definition of "investment company" set forth in Section 3(c)(1) or 3(c)(7) of the Investment Company Act of 1940 (the "**Investment Company Act**") [6] to its customers even if it was engaged by the fund prior to it forming a substantive relationship with such customers, so long as the offer to its customers occurs after the relationship with the customer is established.

C. Rule 506(c) Verification.

(1) The Commission should expand proposed Rule 506(c)(2)(ii)(E) to include investors who have been verified as accredited investors by registered broker-dealers and investment advisers registered with the Commission.

(2) The Commission should add a safe harbor to Rule 506(c)(2) providing, or otherwise clarify, that if a registered broker-dealer or investment adviser registered with the Commission takes the steps necessary to form a "substantive pre-existing relationship" with a potential investor and has received a representation from the investor that it is an accredited investor, such steps are also sufficient for it to have taken "reasonable steps to verify that the purchaser is an accredited investor," as required by Rule 506(c).

(3) The Commission should confirm that when an issuer takes reasonable steps, in accordance with Rule 506(c), to verify that a trust is an accredited investor in accordance with Rule 501(a)(7), it is sufficient, solely with respect to the requirement that the purchase is directed by a sophisticated person, for the issuer to rely on a representation from the trustee to that effect.

We discuss each of the foregoing, in turn, below.

II. Discussion

We strongly support the Commission's proposal to modernize and simplify the Securities Act integration framework for registered and exempt offerings, and hope the Commission will consider the recommendations below, which, if adopted, will significantly reduce the uncertainty and perceived risk among issuers who are offering securities in reliance on Rule 506(c) or who are considering offering securities in reliance on two different exemptions, while preserving investor protections built into the applicable offering exemptions.

A. Integration.

(1) *The Commission should revise proposed Rule 152(a)(1) to clarify that, so long as its conditions are satisfied, an issuer may concurrently engage in an offering in reliance on Rule 506(b) and another offering in reliance on Rule 506(c), even if the*

[6] 15 U.S.C. §80-1 *et seq.*

investors who purchase securities in the Rule 506(c) offering were solicited using general solicitation.

The Proposing Release states:

> Commenters supported allowing concurrent exempt offerings, where one offering permits general solicitation such as Rule 506(c), and the other prohibits general solicitation, such as Rule 506(b). Proposed Rule 152(a)(1) would codify the position that an issuer may conduct such concurrent offerings without integration concerns, provided that for an offering prohibiting general solicitation the issuer has a reasonable belief, based on the facts and circumstances, that the purchasers in each exempt offering were not solicited through the use of general solicitation or the purchasers in each exempt offering established a substantive relationship with the issuer (or a person acting on the issuer's behalf) prior to the commencement of the offering not permitting general solicitation.[7]

This language indicates that the Commission intended for proposed Rule 152(a)(1) to permit an issuer to engage in concurrent exempt offerings, where one offering permits general solicitation, such as Rule 506(c), and the other prohibits general solicitation, such as Rule 506(b), so long as the conditions set forth in proposed Rule 152(a)(1) were satisfied with respect to the offering in reliance on Rule 506(b). However, we are concerned that, as proposed Rule 152(a)(1) is currently drafted, it appears that an issuer may concurrently engage in an offering in reliance on Rule 506(b) and another offering in reliance on Rule 506(c) only if in **both exempt offerings** (i) the purchasers were not solicited through the use of general solicitation or (ii) the purchasers established a substantive relationship with the issuer (or a person acting on the issuer's behalf) prior to the commencement of the offering in reliance on Rule 506(b).

For several reasons, we believe that such an interpretation may not be intended. As an initial matter, such an interpretation would negate the benefit to proposed Rule 152(a) for such concurrent offerings since there would be no benefit to engaging in the Rule 506(c) offering if investors who were solicited by the general solicitation permitted by a Rule 506(c) offering (and with whom neither the issuer nor anyone acting on its behalf had a substantive relationship) could not be sold securities.

Such an interpretation would also be inconsistent with the treatment of concurrent offerings where one of the offerings is exempt and one is not. In such a scenario, proposed Rule 152(a)(1) would permit an issuer filing a Securities Act registration statement with the Commission to conduct a concurrent Rule 506(b) offering if it reasonably believes that the investors in the Rule 506(b) offering were not solicited by the registration statement nor became interested in the concurrent offering through the use of general solicitation in connection with the registered offering.[8] In that case, it is irrelevant that investors purchasing in the registered offering were solicited using general solicitation. We believe a similar treatment is appropriate when an issuer engages in concurrent Rule 506(b) and Rule 506(c) offerings. Namely, in such a case, the issuer should be permitted to

[7] Proposing Release at 17965.

[8] This is consistent with the 2007 release proposing amendments to Regulation D, Revisions of Limited Offering Exemptions in Regulation D, 72 Fed. Reg. 45115 (Aug. 10, 2007) (codified at 17 C.F.R. pts. 200, 230 & 239).

engage in the Rule 506(b) offering even if the investors in the Rule 506(c) offering were solicited for such offering by way of general solicitation.

Lastly, such an interpretation would be inconsistent with prior Commission guidance in the context of two concurrent exempt offerings, one of which permits general solicitation and one of which does not.[9]

Therefore, we believe that such an interpretation may be unintended.[10] Assuming that it is unintended, we recommend that clause (a)(1) of proposed Rule 152 should be revised as follows (text that is <u>double underlined</u> is proposed to be added):

> (1) For an exempt offering for which general solicitation is not permitted, offers and sales will not be integrated with other offerings, if the issuer has a reasonable belief, based on the facts and circumstances, that:
>
> (i) The purchasers in each exempt offering <u>for which general solicitation is not permitted</u> were not solicited through the use of general solicitation; or
>
> (ii) The purchasers in each exempt offering <u>for which general solicitation is not permitted</u> established a substantive relationship with the issuer (or person acting on the issuer's

[9] For example, in Crowdfunding, 80 Fed. Reg. 71387 (Nov. 16, 2015) (codified at 17 C.F.R. pts. 200, 227, 232, 239, 240, 249, 269 & 274), the Commission stated, "an issuer conducting a concurrent exempt offering for which general solicitation is not permitted will need to be satisfied that purchasers in **that offering** were not solicited by means of the offering made in reliance on Section 4(a)(6)." *Id.* at 71392 (emphasis added). That language makes it clear that, when one of the concurrent offerings is of a type for which general solicitation is not permitted, the integration analysis focuses on whether the issuer is satisfied that the investors in "that" specific offering—i.e., the offering for which general solicitation is not permitted (rather than **both** concurrent offerings)—were not brought to such offering via the general solicitation connected to the issuer's other ongoing offering.

Similarly, in Amendments from Small and Additional Issues Exemptions Under the Securities Act (Regulation A), 80 Fed. Reg. 21805 (April 20, 2015) (codified at 17 C.F.R. 200, 230, 232, 239, 240, 249 & 260), the Commission noted that "an issuer conducting a concurrent exempt offering for which general solicitation is not permitted will need to be satisfied that purchasers in **that offering** were not solicited by means of the offering made in reliance on Regulation A, including without limitation any 'testing the waters' communications." *Id.* at 21819 (emphasis added). Again, the evident implication is that the integration analysis turns on whether the general solicitation affected investors in "that offering" —i.e., the offering for which general solicitation is not permitted—rather than **both** concurrent offerings.

Finally, in Exemptions to Facilitate Intrastate and Regional Securities Offerings, 81 Fed. Reg. 83494 (Nov. 21, 2016) (codified at 17 C.F.R. pts. 200, 230, 239, 240, 249, 270 & 275), the Commission stated that, "an issuer conducting a concurrent exempt offering for which general solicitation is not permitted will need to be satisfied that purchasers in that offering were not solicited by means of the offering made in reliance on Rule 147 or new Rule 147A." *Id.* at 83507. In a footnote to that language, the Commission stated, "[f]or a concurrent offering under Rule 506(b), purchasers in the Rule 506(b) offering could not be solicited by means of a general solicitation under Rule 147 or new Rule 147A. The issuer would need an alternative means of establishing how purchasers in the Rule 506(b) offering were solicited. For example, the issuer may have had a preexisting substantive relationship with such purchasers." *Id.* at 83507 n. 182. It is clear from that language that an issuer may engage in two exempt offerings, one of which permits general solicitation (e.g., Rule 147A) and one of which does not (e.g., Rule 506(b)), so long as the purchasers in **only** the offering that does not permit general solicitation were not solicited by the general solicitation.

[10] If it was intended, we urge the Commission to reconsider for the reasons described above.

behalf) prior to commencement of the offering not permitting general solicitation; [. . .]

With these revisions, it will be clear that an issuer may concurrently engage in an offering in reliance on Rule 506(b) and another offering in reliance on Rule 506(c), even if the investors who purchase securities in the Rule 506(c) offering were solicited using general solicitation, so long as the purchasers in the Rule 506(b) offering (i) were not solicited through the use of general solicitation or (ii) established a substantive relationship with the issuer (or a person acting on the issuer's behalf) prior to the commencement of the offering in reliance on Rule 506(b).

(2) *The Commission should revise proposed Rule 152(b)(1) to provide that when an exempt offering for which general solicitation is not permitted is made more than 30 days after the termination of another offering, the two offerings will not be integrated, regardless of whether the purchasers in the exempt offering not permitting general solicitation may have been solicited using general solicitation or had established a substantive relationship with the issuer prior to the commencement of the offering.*

Assuming that the Commission revises proposed Rule 152(a)(1) as recommended above, the current safe harbor in proposed Rule 152(b)(1) would not be useful in a scenario where an issuer terminates an exempt offering for which general solicitation is permitted (e.g., Rule 147A or 506(c)) and commences an offering for which general solicitation is not permitted (e.g., Rule 506(b)). In such a situation, assuming that the Commission revises proposed Rule 152(a)(1) as recommended above, an issuer would never rely on the safe harbor in proposed Rule 152(b)(1) since, if it did, not only would it be required to meet the requirement (found in both proposed Rule 152(a)(1) and proposed Rule 152(b)(1)(i)) that each purchaser (i) is not solicited through the use of general solicitation or (ii) established a substantive relationship with the issuer prior to the commencement of the offering, but it would also, if it relied on proposed Rule 152(b)(1) rather than proposed Rule 152(a)(1), be required to wait 30 days prior to commencing the Rule 506(b) offering (which would not be required if it relied only on proposed Rule 152(a)(1)).

In such a scenario, we believe issuers should have two options: (i) not wait to commence the Rule 506(b) offering, and be required to have a reasonable belief that the purchasers in such offering satisfy the requirements of proposed Rule 152(a)(1) or (ii) terminate the Rule 506(c) offering, and commence the Rule 506(b) offering after waiting 30 days, without being required to satisfy the requirements of proposed Rule 152(b)(1)(i). We agree with the Commission that, "given the accelerating speed and consumption of electronically disseminated information in today's financial marketplace . . . a 30-day time frame is sufficient to mitigate concerns that an exempt offering may condition the market for a subsequent registered offering or undermine the protections of a subsequent exempt offering"[11] As a result, we believe that, even when an offering not permitting general solicitation (e.g., a Rule 506(b) offering) follows an offering permitting general solicitation (e.g., a Rule 506(c) offering), it should not be necessary for the purchasers in the offering not permitting general solicitation to satisfy the requirements set forth in proposed Rule 152(b)(1)(i) so long as there is a 30-day separation between the two offerings. Therefore, we recommend that the Commission revise proposed Rule 152(b)(1) to provide that when an exempt

[11] Proposing Release at 17967.

offering for which general solicitation is not permitted is made more than 30 days after the termination of another offering, the two offerings will not be integrated, regardless of whether the purchasers in the exempt offering not permitting general solicitation may have been solicited using general solicitation or had established a substantive relationship with the issuer prior to the commencement of the offering.

If the Commission agrees with our recommendation, we would suggest that the most straightforward means of accomplishing this revision is to delete clauses (i) and (ii) of proposed Rule 152(b)(1).

(3) *The Commission should include an additional safe harbor in proposed Rule 152(b) providing that any offering commenced in reliance on an exemption that does not permit general solicitation can be continued in reliance on an exemption that does permit general solicitation. If the Commission declines to include that new safe harbor, we believe it should clarify that an issuer can accomplish the same result pursuant to the safe harbor in proposed Rule 152(b)(4).*

In the Proposing Release, the Commission asks if the integration framework should also include provisions applying the general principal to particular fact patterns.[12] We believe that the safe harbor in proposed Rule 152(b)(4) is helpful, but believe that it would be beneficial to issuers for the Commission to provide an additional safe harbor regarding one scenario that can be expected to arise with regularity—namely, an issuer commencing an offering in reliance on Rule 506(b) and desiring to continue it in reliance on Rule 506(c). This may occur because the issuer initially believes that it can raise the capital it needs without engaging in general solicitation, but subsequently determines that it is unable to raise that capital without engaging in general solicitation.[13] In such a scenario, we believe that the issuer should be able to seamlessly, and using, if it desires, the same (or substantially identical) offering materials, continue the offering in reliance on Rule 506(c).

We believe that an additional safe harbor permitting an issuer that has commenced an offering in reliance on Rule 506(b) to continue such offering in reliance on Rule 506(c) would be consistent with the Commission's guidance in the 2013 release implementing Rule 506(c) (the "**2013 Release**").[14] In that release, the Commission stated:

> [F]or an ongoing offering under Rule 506 that commenced before the effective date of Rule 506(c), the issuer may choose to continue the offering after the effective date in accordance with the requirements of either Rule 506(b) or Rule 506(c). If an issuer chooses to continue the offering in accordance with the requirements of Rule 506(c), any general solicitation that occurs after the effective date will not affect the exempt status of offers and sales of securities that occurred prior to the effective date in reliance on Rule 506(b).[15]

[12] *Id.* at 17972.
[13] This may also occur when an issuer intends to conduct an offering in reliance on Rule 506(b), but, after the commencement of the offering, an employee of the issuer inadvertently engages in activity that may be considered a general solicitation, thereby rendering the issuer unable to continue with its Rule 506(b) offering.
[14] Eliminating the Prohibition Against General Solicitation and General Advertising in Rule 506 and Rule 144A Offerings, 78 Fed. Reg. 44771 (July 24, 2013) (codified at 17 C.F.R. pts. 230, 239 & 242).
[15] *Id.* at 44776.

While the Commission did not explain its reason for limiting that guidance to offerings that commenced prior to the effective date of Rule 506(c), it may have been because of concerns regarding integration. Since the Commission is now proposing to amend such rules, we believe it is the appropriate opportunity to expand such guidance to include any offering that commenced in reliance on Rule 506(b), regardless of when the offering commenced. In order to do so, we believe the Commission should include an additional safe harbor in proposed Rule 152(b) providing that any offering that commenced in reliance on an exemption that does not permit general solicitation can be continued in reliance on an exemption that does permit general solicitation. As we noted above, such a safe harbor would not raise any investor protection concerns since the issuer will, pursuant to Rule 506(c), take reasonable steps to verify that all investors whose offers to purchase securities were accepted following a general solicitation are accredited investors.

In addition, the Commission should clarify that when using such safe harbor:

- the issuer is not required to take any action to "terminate" the Rule 506(b) offering;
- investors who were solicited in connection with the offering in reliance on Rule 506(b) can have their offers to invest accepted in an offering in reliance on Rule 506(c), and it is not necessary to provide such investors with any additional or different offering materials; and
- in the offering in reliance on Rule 506(c), the issuer may continue to use the same (or substantially identical) offering materials that were provided to investors in the offering that commenced in reliance on Rule 506(b).

If the Commission does not include that new safe harbor, we believe it should clarify that an issuer can accomplish the same result, pursuant to proposed Rule 152(b)(4), by terminating the Rule 506(b) offering and simultaneously commencing the Rule 506(c) offering (i) without being required to take any action to "terminate" the Rule 506(b) offering, (ii) if it desires, using the same offering (or substantially identical) materials and (iii) without being required to recirculate such offering materials to investors who received them in connection with the Rule 506(b) offering.

(4) *The Commission should revise proposed Rule 152(c)(ii) to clarify that an issuer can seamlessly terminate an offering in reliance on one exemption and simultaneously commence an offering of those securities in reliance on another offering exemption. In addition, the Commission should state that it is not necessary for an issuer to use different offering materials for offerings that rely on different exemptions.*

We believe that proposed Rule 152(c) should permit an issuer to seamlessly terminate an offering in reliance on one exemption and simultaneously commence an offering in reliance on another exemption, and therefore believe that proposed Rule 152(c)(1)(ii) should be clarified as follows (text that is <u>double underlined</u> is proposed to be added):

> (ii) The issuer and its agents ceased efforts to make further offers to sell the issuer's securities <u>under such offering</u>.

This clarification is important because if an issuer determines to terminate an offering of securities in reliance on one exemption and simultaneously commence an offering of securities in reliance on another exemption, the issuer likely would not be able to say that it has "ceased efforts to make further offers to sell" its securities; rather, it could say only that it has ceased efforts to sell securities in reliance on one exemption (while simultaneously commencing efforts to sell securities in reliance on a different exemption).

In addition, while the Proposing Release notes that "ceasing efforts to make further offers to sell the issuer's securities" includes the distribution of any offering materials,[16] we urge the Commission to recognize that the offering materials for one exempt offering may be identical (or substantially similar) to the offering materials for another exempt offering (or the same offering materials may be used for two concurrent exempt offerings) and that requiring an issuer to create new offering materials for the subsequent offering would increase costs without benefiting investors. Therefore, we urge the Commission to state that it is not necessary for an issuer to use different offering materials for offerings that rely on different exemptions.

(5) *The Commission should clarify that, consistent with the principle behind proposed Rule 152(a)(1), general solicitations by the issuer in connection with a primary offering in reliance on Rule 506(c) or another offering that permits general solicitation will not be integrated with an investor's secondary offering in reliance on Section 4(a)(7), so long as (i) the investors in the offering in reliance on Section 4(a)(7) were not solicited through the use of general solicitation or (ii) the purchasers established a substantive relationship with the issuer or the investor (or a person acting on behalf of the issuer or the investor) prior to the commencement of the offering in reliance on Section 4(a)(7).*

Section 4(a)(7) of the Securities Act, which was adopted as part of the Fixing America's Surface Transportation (FAST) Act,[17] exempts from registration a resale of securities by investors so long as, among other conditions, neither the seller nor any person acting on the seller's behalf offers or sells securities by any form of general solicitation. In connection with certain sales by an investor pursuant to Section 4(a)(7), it is possible that the issuer will assist the investor in identifying potential purchasers for the investor. It is also possible that, at or about the same time, the issuer will engage in a primary offering in reliance on Rule 506(c) or another offering that permits general solicitation. In order to avoid any concern that the issuer's general solicitation in connection with its primary offering would be integrated with the investor's secondary offering in reliance on Section 4(a)(7), resulting in such general solicitation precluding the investor from offering securities in reliance on Rule Section 4(a)(7), we recommend that the Commission clarify that, consistent with the principle behind proposed Rule 152(a)(1), general solicitations by the issuer in connection with a primary offering will not be integrated with the investor's secondary offering in reliance on Section 4(a)(7) so long as (i) the investors in the offering in reliance on Section 4(a)(7) were not solicited through the use of general solicitation or (ii) the purchasers established a substantive relationship with the issuer or the investor (or a person acting on behalf of the issuer or the investor) prior to the commencement of the offering in reliance on Section 4(a)(7).

[16] Proposing Release at 17969 n. 102.
[17] Pub. L. No. 114-94 (2015).

(6) *The Commission should not enact proposed Rule 906. We recommend that the Commission address the uncertainty among market participants regarding whether it is possible to conduct concurrent Regulation S and Rule 506(c) offerings by revising Rule 902 to expressly provide that the prohibition on "directed selling efforts" is not applicable when the Regulation S offering is made concurrently with an offering (a) in reliance on an exemption that permits general solicitation, so long as the issuer does not engage in such general solicitation for the purpose of conditioning the market in the United States for any securities being offered in reliance on Regulation S or (b) registered under the Securities Act. We also recommend that the Commission clarify that the issuer is not required to provide evidence for its intent. In addition, we recommend that the Commission state that concurrent Rule 506(c) and Regulation S offerings will not be integrated even if the issuer uses the same (or substantially identical) offering materials for the offerings.*

We appreciate the Commission's desire to provide a clear framework that an issuer may use to conduct an exempt offering that permits general solicitation (e.g. Rule 506(c)) concurrently with an offshore offering in reliance on Regulation S without concern that such general solicitation may constitute "directed selling efforts" under Regulation S.[18] We note that in the 2013 Release, the Commission stated:

> In the Proposing Release, we noted that the mandate in Section 201(a) that the Commission amend Rule 506 and Rule 144A to permit the use of general solicitation in transaction under those rules has raised questions from some commenters regarding the impact of the use of general solicitation on the availability of the Regulation S safe harbor for concurrent unregistered offerings inside and outside the United States . . . . We expressed our view on this issue in the Proposing Release, which we are reaffirming in this release. Concurrent offshore offerings that are conducted in compliance with Regulation S will not be integrated with domestic unregistered offerings that are conducted in compliance with Rule 506 or Rule 144A, as amended.[19]

We believe the reason "there may be some uncertainty among market participants about whether it is possible to conduct concurrent Regulation S and Rule 506(c) offerings,"[20] is because while, in the 2013 Release, the Commission acknowledged that some commenters had raised questions regarding the impact of the use of general solicitation on the availability of the Regulation S safe harbors for concurrent unregistered offerings inside and outside the United States, the statement in the 2013 Release quoted above did not expressly address such concerns. In particular, the Commission did not expressly address whether there are circumstances in which general solicitation relating to a Rule 506(c) offering may constitute directed selling efforts that would preclude a concurrent Regulation S offering. In addition, later statements by the staff of the Division of Corporation Finance (the "**Staff**") and the Commission may have contributed to the

[18] Proposing Release at 17970.
[19] 2013 Release at 44786; *see also* nn. 176-77.
[20] Proposing Release at 17970.

uncertainty. For example, the Staff stated that the amendments to Rule 144A permitting the use of general solicitation did not change how directed selling efforts under Regulation S are analyzed in concurrent Rule 144A and Regulation S offerings.[21] In addition, in the 2019 concept release on exemptions,[22] the Commission indicated that when an issuer engages in concurrent offerings using general solicitation under Rule 506(c) to U.S. investors and under Regulation S, it could not use the same offering materials for both offerings since, if it did, "the Regulation S materials would then include activity undertaken for the purpose of conditioning the market in the U.S."[23] Similarly, the Proposing Release refers to "the requirement that separate offering materials be used in each [i.e., the Rule 506(c) and the Regulation S] offering."[24]

We believe it is critical that the Commission address this uncertainty clearly and unequivocally so that issuers will have clarity regarding the steps they need to take to conduct concurrent Rule 506(c) and Regulation S offerings. However, we believe proposed Rule 906, which is intended to protect against flowback of securities initially placed outside the United States, is unnecessary because current Regulation S, coupled with the overlay of Section 4(a)(3), already provides for a tailored distribution compliance period regime designed to protect against flowback whose onerousness varies directly to the likelihood of flowback. Current Rule 905 of Regulation S reflects the determination that domestic equity securities are the only securities offered under Regulation S with a flowback risk that warrants treatment as "restricted securities," thus precluding their free public resale in the United States for six months or one year, as applicable. Proposed Rule 906 would in large part conflate the consequences of general solicitation with the flowback risk for domestic securities—a conflation unsupported by any particular evidence. In addition, and perhaps most significantly, the Commission's statement in the 2013 Release quoted above, as well as similar statements noted in footnote 177 to the 2013 Release, indicate that an issuer is permitted to engage in concurrent offerings under Rule 506(c) and Regulation S, and the Commission has never previously indicated that issuers were required to impose additional transfer restrictions or that issuers were otherwise required to take any specific action to ensure that any general solicitation under the Rule 506(c) offering would not constitute directed selling efforts under the Regulation S offering. Therefore, we believe the Commission should not enact proposed Rule 906.

We believe the proposed amendment to Rule 902 (requiring that an issuer that is engaging in general solicitation in connection with an exempt offering not undertake such activity for the purpose of conditioning the market in the United States for any securities being offered in reliance on Regulation S), is an appropriate application of Preliminary Note 2 to Regulation S, which provides that "any transaction that . . . although in technical compliance with these rules, is part of a plan or scheme to evade the registration provisions of the Act" requires registration.[25] However, we believe that the Commission should clarify that the issuer is not required to provide evidence

[21] Compliance and Disclosure Interpretations, Question 138.04 (Nov. 13, 2013), https://www.sec.gov/divisions/corpfin/guidance/securitiesactrules-interps htm.
[22] Concept Release on Harmonization of Securities Offering Exemptions, 84 Fed. Reg. 30460 (June 26, 2019) (codified at 17 C.F.R. pts. 210, 227, 230, 239, 240, 270, 274 & 275).
[23] *Id.* at 30511 n. 519.
[24] Proposing Release at 17970.
[25] Preliminary Note 2 to Regulation S—Rules Governing Offers and Sales Made Outside the United States Without Registration Under the Securities Act of 1933, 55 Fed. Reg. 18322, May 2, 1990, as amended at 62 Fed. Reg. 53954, Oct. 17, 1997; 63 Fed. Reg. 9642, Feb. 25, 1998 (codified at 17 C.F.R. pts. 901-05).

for its intent since, except in the most egregious examples that would be addressed by Preliminary Note 2, it is difficult to know what form that evidence would take.

Therefore, we recommend that the Commission address the uncertainty among market participants regarding whether it is possible to conduct concurrent Regulation S and Rule 506(c) offerings by revising Rule 902 to expressly provide that the prohibition on "directed selling efforts" is not applicable when the Regulation S offering is made concurrently with an offering (a) in reliance on an exemption that permits general solicitation so long as the issuer that does not engage in such general solicitation for the purpose of conditioning the market in the United States for any securities being offered in reliance on Regulation S or (b) registered under the Securities Act. We also recommend that the Commission clarify that that the issuer is not required to provide evidence for its intent.

In addition, as stated above, we believe that an issuer should be permitted to use the same (or substantially identical) offering materials for concurrent exempt offerings since doing so will reduce issuer costs without increasing any risks to investors.[26] Therefore, we believe it is important for the Commission to state that concurrent Rule 506(c) and Regulation S offerings will not be integrated even if the issuer uses the same (or substantially identical) offering materials for the offerings.

(7) *The Commission should amend Rule 502(c) to provide that a general solicitation shall be deemed to not have occurred with respect to an offering for which general solicitation is prohibited if all of the purchasers in such offering (i) were not solicited through the use of general solicitation or (ii) established a substantive relationship with the issuer (or a person acting on the issuer's behalf) prior to the commencement of the offering.*

The Proposing Release asks whether a provision similar to that in proposed Rule 152(b)(1)(i) would be more appropriate in Rule 502(c) of Regulation D concerning purchasers in offerings in which general solicitation is not permitted.[27] We believe that it would be appropriate to include in Rule 502(c) a provision that a general solicitation shall be deemed to not have occurred with respect to an offering for which general solicitation is prohibited if all of the purchasers in such offering (i) were not solicited through the use of general solicitation or (ii) established a substantive relationship with the issuer (or a person acting on the issuer's behalf) prior to the commencement of the offering.

We recommend that the Commission adopt such a change because, as stated above, we believe the Commission intends to permit an issuer to conduct an offering in reliance on Rule 506(b) concurrently with an offering in reliance on Rule 506(c) that includes general solicitation (so long as the conditions to proposed Rule 152(a)(1) are satisfied).[28] Assuming that is the case, the Commission should also permit an issuer to engage solely in an offering in reliance on Rule 506(b) (i.e., without a concurrent offering in reliance on Rule 506(c)) even if there is concurrent general solicitation, so long as the conditions in proposed Rule 152(a)(1) are satisfied. Put differently, if

[26] *Cf. supra* Section II.A(3).
[27] *See* Proposing Release at 17972 (Request for Comment No. 7).
[28] *See supra* Section II.A(1).

the criteria in proposed Rule 152(a)(1) are satisfied with respect to a potential participant in a Rule 506(b) offering, the issuer's ability to conduct the Rule 506(b) offering should not depend on whether a separate group of offerees are generally solicited in a separate, but concurrent, offering.

We believe that permitting an issuer to engage in an offering in reliance on Rule 506(b) if there is general solicitation even if the issuer does not actually engage in a Rule 506(c) offering (so long as the conditions in proposed Rule 152(a)(1) are satisfied) would be consistent with the guidance provided in the 2013 Release in which the Commission noted that whether a general solicitation is deemed to have occurred (thereby precluding reliance on Rule 506(b)) depends on whether, "the purchasers became interested in the offering because of, or through, the general solicitation, and not through some means other than the general solicitation, such as through a substantive, pre-existing relationship with the company or direct contact by the company or its agents outside of the general solicitation."[29]

Under the approach we recommend, an issuer could (i) engage in an offering in reliance on Rule 506(b) while engaging in general solicitation so long as the purchasers in the Rule 506(b) offering were not solicited through the use of general solicitation or the purchasers established a substantive relationship with the issuer (or a person acting on the issuer's behalf) prior to the commencement of the Rule 506(b) offering[30] or (ii) engage in an offering in reliance on Rule 506(c) and engage in general solicitation so long as the issuer took reasonable steps to verify the purchasers of securities sold in the offering. We believe that such an approach is entirely consistent with the underlying policy reflected in proposed Rule 152(a), namely, that an issuer may engage in general solicitation concurrently with an offering in reliance on Rule 506(b) so long as the purchasers in the Rule 506(b) offering were not solicited through the use of general solicitation or the purchasers established a substantive relationship with the issuer (or a person acting on the issuer's behalf) prior to the commencement of Rule 506(b) offering.

B. Substantive pre-existing relationships.

(1) *The Commission should state that a broker-dealer or investment adviser may offer interests in private funds that rely on the exclusions from the definition of "investment company" set forth in Section 3(c)(1) or 3(c)(7) of the Investment Company Act to its customers even if it was engaged by the fund prior to it forming a substantive relationship with such customers, so long as the offer to its customers occurs after the relationship with the customer is established.*

Proposed Rule 152(a)(1) requires that, for an exempt offering for which general solicitation is not permitted, each purchaser either (i) was not solicited through the use of general solicitation or (ii) established a substantive relationship with the issuer (or a person acting on the issuer's behalf)

[29] 2013 Release at 44783 n. 142.

[30] While it may be unlikely that an issuer would engage in a general solicitation if it would not use the general solicitation to solicit investors with whom it (or a person acting on its behalf) did not have a substantive pre-existing relationship, this guidance would permit issuers to engage in an offering in reliance on Rule 506(b) without the ever-present concern that an inadvertent statement that may constitute a general solicitation may occur, resulting in the issuer's inability to continue the offering. The elimination of such concern would be a significant benefit to issuers and would not raise investor protection concerns.

prior to the commencement of the offering for which general solicitation is not permitted.[31] With respect to the latter clause, the Proposing Release states that the Commission views a "pre-existing" relationship as one that the issuer has formed with the offeree prior to the commencement of the securities offering or, alternatively, that was established through another person (e.g., a broker-dealer or investment adviser) prior to that person's participation in the offering.[32] The Proposing Release also states that, "[g]enerally, whether a 'pre-existing, substantive relationship' exists turns on procedures established by broker-dealers in connection with their customers. This is because traditional broker-dealer relationships require that a broker-dealer deal fairly with, and make suitable recommendations to, customers, and thus implies that a substantive relationship exists between the broker-dealer and its customers."[33] We believe that once a broker-dealer or investment adviser develops that relationship, it should be permitted to offer securities to its customer, even if the broker-dealer or investment adviser was engaged by the issuer prior to the date on which the broker-dealer or investment adviser developed its relationship with the customer, so long as the offer to its customers occurs after the relationship with the customer is established.

While we believe this is the appropriate result for all offerings, we consider it especially important in the context of offerings for private funds that rely on the exclusions from the definition of "investment company" set forth in Section 3(c)(1) or 3(c)(7) of the Investment Company Act, because such funds engage in continuous offerings. Because the offering may continue for many years, a broker-dealer or investment adviser may desire to offer interests in the fund to customers with whom it establishes relationships after it has been engaged by the fund. We believe it is appropriate for the broker-dealer or investment adviser to be permitted to do so, so long as the offer to its customers occurs after the relationship with the customer is established.

The Proposing Release notes that certain offerings by private funds that rely on the exclusions from the definition of "investment company" set forth in Section 3(c)(1) or 3(c)(7) of the Investment Company Act posted on a website platform may be able to rely on a limited staff accommodation set forth in the No-Action Letter to Lamp Technologies, Inc. (the "**Lamp NAL**") with respect to the timing of the formation of a relationship.[34] However, because it is not entirely clear whether, and to what extent, the guidance provided in the Lamp NAL must be limited to its particular facts, we believe it is important that the Commission state that a broker-dealer or investment adviser may offer interests in private funds that rely on the exclusions from the definition of "investment company" set forth in Section 3(c)(1) or 3(c)(7) of the Investment Company Act to its customers even if it was engaged by the fund prior to it forming the substantive relationship with such customer, so long as the offer to its customers occurs after the relationship with the customer is established.

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[31] *See* Proposing Release at 18042-43. We note that while proposed Rule 152(a)(1)(ii) includes the parenthetical phrase "(or person acting on the issuer's behalf)," proposed Rule 152(b)(1)(i)(B) does not include that phrase. We believe that the discrepancy is unintentional and recommend that, if the Commission retains proposed Rule 152(b)(1)(i)(B), it include that parenthetical. In addition, proposed Rule 152(a)(1) includes a "reasonable belief" standard, while proposed Rule 152(b)(1) does not; we believe the Commission should address that discrepancy by including a "reasonable belief" standard in proposed Rule 152(b)(1).

[32] *Id.* at 17966.

[33] *Id.* at 17966 n. 72.

[34] *See id.* at 17966 n. 71 (citing Lamp Technologies, Inc., SEC No-Action Letter, 1997 SEC No-Act. LEXIS 638 1-12 (May 29, 1997)).

C. Rule 506(c) Verification.

(1) *The Commission should expand proposed Rule 506(c)(2)(ii)(E) to include investors who have been verified as accredited investors by registered broker-dealers and investment advisers registered with the Commission.*

Proposed Rule 506(c)(2)(ii)(E) provides that an issuer will be deemed to have taken reasonable steps to verify that purchasers are accredited investors if, in regard to any person that the issuer has previously verified as an accredited investor in accordance with paragraph (c)(2)(ii) of Rule 506, the issuer obtains a written representation from such person at the time of sale that he or she qualifies as an accredited investor, so long as the issuer is not aware of information to the contrary.[35]

We believe that the proposed rule is helpful, but that its impact will be severely curtailed unless the Commission expands its coverage to include registered broker-dealers and investment advisers registered with the Commission. Those parties are far more likely than any single issuer (i) to have taken reasonable steps to verify that an investor is an accredited investor, (ii) to be involved in multiple offerings and (iii) to retain such records for future offerings. As noted above, the Proposing Release acknowledges the special role that broker-dealers play in forming substantive relationships with their clients. Such relationships place broker-dealers in the best position to have taken reasonable steps to verify that such customers are accredited investors.[36] Similarly, investment advisers have a fiduciary duty to understand their customers' investment objectives and financial situation. Therefore, we recommend that proposed Rule 506(c)(2)(ii)(E) should be amended as follows (text that is <u>double underlined</u> is proposed to be added):

> (E) In regard to any person that the issuer, <u>any registered broker-dealer or investment adviser registered with the Securities and Exchange Commission</u> has previously verified as an accredited investor in accordance with this paragraph (c)(2)(ii), so long as the issuer, <u>the broker-dealer or investment adviser, as applicable,</u> is not aware of information to the contrary, obtaining a written representation from such person at the time of sale that he or she qualifies as an accredited investor.

The Proposing Release also inquires as to an appropriate time limit on the utilization of this verification method.[37] In response, we propose the imposition of a three-year limit that begins running as of the date upon which the investor's status is verified, as we believe this duration strikes a balance between the Commission's objective to streamline the verification process on the one hand, and, on the other hand, the reality that financial circumstances can change over time.

(2) *The Commission should add a safe harbor to Rule 506(c)(2) providing, or otherwise clarify, that if a registered broker-dealer or investment adviser registered with the Commission takes the steps necessary to form a "substantive*

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[35] *Id.* at 18045.
[36] *See supra* Section II.B(1) (quoting Proposing Release at 17966 n. 72).
[37] Proposing Release at 17981 (Request for Comment No. 35).

pre-existing relationship" with a potential investor and has received a representation from the investor that it is an accredited investor, such steps are also sufficient for it to have taken "reasonable steps to verify that the purchaser is an accredited investor," as required by Rule 506(c).

The Proposing Release states that an issuer's receipt of a representation from an investor as to his or her accredited status could meet a Rule 506(c) offering's "reasonable steps" to verify requirement if the issuer reasonably takes into consideration a prior substantive relationship with the investor.[38] The Proposing Release also explains that a "substantive" relationship is one in which the issuer (or a person acting on its behalf, such as a registered broker-dealer or investment adviser registered with the Commission) has sufficient information to evaluate, and does, in fact, evaluate, an offeree's financial circumstances and sophistication in determining their status as an accredited or sophisticated investor.[39]

Read together, it seems reasonable to infer that the Commission recognizes that if a registered broker-dealer or investment adviser has a "substantive pre-existing relationship" with a potential investor, the steps that were necessarily taken by such broker-dealer or investment adviser in forming such a relationship should also be sufficient to satisfy Rule 506(c)'s requirement that the broker-dealer or investment adviser has taken "reasonable steps to verify that the purchaser is an accredited investor."

We believe that such recognition is warranted and that it would be helpful for the Commission to add a safe harbor to Rule 506(c)(2) providing, or otherwise clarify, that if a registered broker-dealer or investment adviser takes the steps necessary to form a "substantive pre-existing relationship" with a potential investor and has received a representation from the investor that it is an accredited investor, such steps are also sufficient for it to have taken "reasonable steps to verify that the purchaser is an accredited investor," as required by Rule 506(c).

(3) *The Commission should confirm that when an issuer takes reasonable steps, in accordance with Rule 506(c), to verify that a trust is an accredited investor in accordance with Rule 501(a)(7), it is sufficient, solely with respect to the requirement that the purchase is directed by a sophisticated person, for the issuer to rely on a representation from the trustee to that effect.*

Pursuant to Rule 501(a)(7), a trust is an accredited investor if (i) it has total assets in excess of $5 million, (ii) it is not formed for the specific purpose of acquiring the securities offered and (iii) its purchase is directed by a sophisticated person as described in Rule 506(b)(2)(ii). While we believe there is sufficient understanding of the steps that are required to be taken to satisfy the requirement pursuant to Rule 506(c)(2)(ii) to verify the first two conditions of Rule 501(a)(7), we believe that, given the subjectivity of the third condition and, more importantly, the fact that such condition is not present in Rule 501(a)(3), it should be sufficient for an issuer to rely on a representation of sophistication from the person who is directing such trust, as long as the issuer does not have any reason to believe the contrary. Therefore, we believe that the Commission should confirm that when an issuer takes reasonable steps, in accordance with Rule 506(c), to verify that a trust is an

[38] *Id.* at 17981.
[39] *Id.* at 17966.

accredited investor in accordance with Rule 501(a)(7), it is sufficient, solely with respect to the requirement that the purchase is directed by a sophisticated person, for the issuer to rely on a representation from the trustee to that effect.

We appreciate the opportunity to comment on the proposed amendments to the exempt offering framework. If the Commission or the staff of the Commission have any questions or wish to discuss the matters mentioned in this letter, please contact Jonathan Adler at [redacted] or [redacted].

Very truly yours,

Fried, Frank, Harris, Shriver & Jacobson LLP

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