

**MEMO# 21454**

August 9, 2007

## **SEC Proposes Revisions To Regulation D; August 30th Conference Call**

[21454]

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TO: CLOSED-END INVESTMENT COMPANY COMMITTEE No. 28-07  
INVESTMENT ADVISERS COMMITTEE No. 16-07  
SEC RULES COMMITTEE No. 63-07  
SMALL FUNDS COMMITTEE No. 32-07 RE: SEC PROPOSES REVISIONS TO REGULATION D;  
AUGUST 30TH CONFERENCE CALL

The Securities and Exchange Commission recently published for comment revisions to several rules under the Securities Act of 1933 applicable to private offerings. [1] In particular, the SEC proposed new Rule 507, which contains a new exemption from registration under the Securities Act for offers and sales to “large accredited investors.” Issuers would be permitted to publish a limited announcement of Rule 507 offerings. Hedge funds and other private pooled investment vehicles that rely on Sections 3(c)(1) or 3(c)(7) of the Investment Company Act would not be permitted to sell their securities in reliance on Rule 507.

The SEC also proposed revising the definition of the term “accredited investor” to reflect recent developments and solicited further comment on proposed Rules 216 and 509 under the Securities Act. Rules 216 and 509 would establish a new category of accredited investor, “accredited natural person.” Under the proposed rules, only those individuals that qualify as “accredited natural persons” would be permitted to invest in private pooled investment vehicles that rely on Sections 3(c)(1) or 3(c)(7). These rules initially were proposed for comment in December 2006. [2] Finally, the SEC proposed shortening the length of time required by the integration safe harbor for Regulation D offerings, and applying uniform disqualification provisions throughout Regulation D. The Release is summarized below.

Comments on the Release are due to the SEC on October 9th. The Institute will hold a conference call to discuss the Release and the Institute’s comments thereon on Thursday, August 30th at 3:00 EST. If you plan on participating in the call, please let Kathy Craft know via email ([tlegal@ici.org](mailto:tlegal@ici.org)) as soon as possible but no later than August 28th. If you are unable to participate on the call but have comments on the Release, please provide them

prior to the call to Dorothy Donohue by phone (202) 218-3563 or email ([ddonohue@ici.org](mailto:ddonohue@ici.org)). The dial-in number for the call is 888-390-3110 and the pass code is 69176.

## **Proposed Revisions to Regulation D**

### **A. Proposed Rule 507 - Exemption for Limited Offers and Sales to Large Accredited Investors**

Proposed Rule 507 would create a new exemption from registration under the Securities Act for offers and sales to a new category of investors called “large accredited investors.”

Large accredited investors would consist of the same categories of entities and individuals that qualify for accredited investor status under existing Rule 506 but with higher dollar thresholds (for investors subject to such thresholds). Legal entities, such as corporations and business trusts, that currently are considered accredited investors if their assets exceed \$5 million would be required to have \$10 million of investments to qualify as large accredited investors. Registered investment companies and other legal entities that currently are not subject to dollar amount thresholds to qualify as accredited investors, would qualify as large accredited investors. Individuals would be required to own \$2.5 million in investments or have annual income of \$400,000 (or \$600,000 with a spouse) in the last two years and expect to maintain the same income level in the current year to qualify as large accredited investors. [\[3\]](#)

Issuers would be permitted to publish a limited announcement of a Rule 507 offering. The announcement would be required to state prominently that: sales would be made to large accredited investors only; no money or other consideration is being solicited or would be accepted through the announcement; the securities had not been registered with or approved by the SEC; and the securities are being offered pursuant to an exemption. At the issuer’s option, the announcement also could contain the following additional information: the issuer’s name and address; a description of the issuer in 25 or fewer words; the name, type, number, price, and aggregate amount of securities being offered; a brief description of the securities; a description of the meaning of “large accredited investor”; any suitability standards and minimum investment requirements for prospective purchasers in the offering; and the name, postal or email address, and telephone number of a contact person for additional information. Under the proposal, issuers could only include announcements in a written medium such as a newspaper or the Internet, not in radio or television broadcasts.

Proposed Rule 507 would permit an issuer to provide information in addition to the limited announcement only if the issuer reasonably believes that the prospective purchaser is a large accredited investor. This additional information could be provided in writing, orally, or in a database that could be accessed only by large accredited investors.

As stated above, under the proposal, private pooled investment vehicles that rely on Sections 3(c)(1) or 3(c)(7) of the Investment Company Act would be precluded from selling their securities in reliance on Rule 507. As such, they would not be permitted to publish the announcements described above.

### **B. Proposed Revisions Relating to Definition of “Accredited Investor”**

Under the proposal, Rule 501(a) of Regulation D would be revised to add an “investments-owned” standard as an alternative to the current income and assets standards. A legal entity currently required to have \$5 million in assets to be considered an accredited

investor also would be considered to be an accredited investor if it has \$5 million in investments. Individuals would be considered to be accredited investors if they have \$750,000 in investments, net worth of \$1 million, or annual income of \$200,000 (or \$300,000 with a spouse). The Release notes that the addition of an investments-owned standard may simplify compliance burdens for companies because that standard may be assessed more easily than the current standards.

### **C. Definition of Accredited Natural Person in Proposed Rules 216 and 509**

The Release notes that in the Private Pooled Investment Vehicle Release, the SEC proposed limiting investments by individuals in pooled investment vehicles under Sections 3(c)(1) or 3(c)(7) of the Investment Company Act to “accredited natural persons.” Accredited natural persons would be defined as natural persons with: (i) individual net worth or joint net worth with a spouse of \$1 million at time of purchase; or (ii) individual net income that exceeds \$200,000 (or joint income with a spouse that exceed \$300,000) in each of the two most recent years and who has a reasonable expectation of reaching the same income level in the year of investment; and (iii) individual (or joint ownership with a spouse) of at least \$2.5 million in investments.

The Release notes that the SEC received numerous comments arguing that the proposed dollar amount of the investments standard would inappropriately limit access to private pooled investment vehicles. [\[4\]](#) The Release states that in light of those comments, the SEC is soliciting additional comment as to whether: (i) the proposed definition of accredited natural person should be revised to include alternative income and investment standards similar to those used in Rule 507’s proposed large accredited investor standard (individual income of \$400,000 or joint income of \$600,000 or investments of \$2.5 million). The Release also seeks comment on whether lower or higher income and/or investment standards would be more appropriate.

### **D. Future Inflation Adjustments**

Under the proposal, all dollar-amount thresholds set forth in Rule 501 of Regulation D would be adjusted to reflect any changes in the value of the Personal Consumption Exemption Chain-Type Price Index starting on July 1, 2012 and every five years thereafter.

### **E. Adding Categories of Entities to List of Accredited and Large Accredited Investors**

To reduce uncertainty and promote more efficient private capital formation, the proposal would expand the list of legal entities that are accredited investors to include limited liability companies, Indian tribes, labor unions, governmental bodies, and other legal entities with similar legal attributes that otherwise satisfy the relevant standards.

### **F. Proposed Revisions to Regulation D Integration Safe Harbor**

Under the proposal, Rule 502(a)’s integration safe harbor would be amended. In particular, a ninety day requirement would replace the current six month requirement so that offers and sales more than ninety days before a Regulation D offering or more than ninety days after the completion of a Regulation D offering would not be considered to be part of the same offering. The Release seeks comment on whether the interaction between the announcement permitted by proposed Rule 507 and the proposed ninety-day integration safe harbor would present opportunities for abuse. It also asks whether Rule 507 should prohibit an issuer from using announcements to test the waters before deciding whether to undertake either a registered public offering or an unregistered exempt offering under

Regulation D.

## **G. Disqualification Provisions**

Under proposed Rule 502(e), an issuer could not rely on Regulation D if any “covered person,” including the issuer, its director, executive officer, general partner, or 20 percent beneficial owner, is “disqualified.” For example, covered persons would be disqualified if convicted of a criminal offense in the last ten years that was in connection with the offer, purchase, or sale of a security.

Dorothy M. Donohue  
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### **endnotes**

[1] See SEC Release Nos. 33-8828, IC-27922 (August 3, 2007) (“Release”). The Release is available on the SEC’s website at <http://www.sec.gov/rules/proposed/2007/33-8828.pdf>.

[2] See Institute [Memorandum](#) to SEC Rules Committee No. 3-07, Closed-End Investment Company Committee No. 1-07, Investment Advisers Committee No. 1-07, Small Funds Committee No. 1-07 [20772], dated January 9, 2007 (summarizing the SEC’s December 2006 Release) (“Private Pooled Investment Vehicle Release”).

[3] The current accredited investor standard for individuals is \$1 million of net worth or annual income of \$200,000 (or \$300,000 with a spouse).

[4] In its comment letter, the Institute strongly supported the proposed dollar amount of the investment standard, reasoning that private pooled investment vehicles only should be available to investors with the sophistication to identify, analyze, and bear the risks of investing in these complex, illiquid, opaque investments. See Institute [Memorandum](#) to SEC Rules Members No. 32-07, Closed-End Investment Company Members No. 17-07, Investment Adviser Members No. 7-07, Small Funds Members No. 23-07 [20949], dated March 13, 2007 (summarizing the Institute’s comment letter).