Kirkland & Ellis
Washington, D.C.

November 6, 1981

BY HAND

George A. Fitzsimmons, Secretary
Securities and Exchange Commission
500 N. Capitol Street, N.W.
Washington, D.C. 20549

Re: Securities Act Release No. 6339
File No. S7-891

Dear Sir:

I respectfully submit the following comments on Release No. 6339 under the Securities Act of 1933 ("1933 Act") concerning proposed Regulation D. These comments reflect my personal views as to the issues raised in the Release and do not reflect the views of the above firm or any other lawyers in the firm.

I recognize that these comments are being submitted beyond the Commission's due date for comments and I apologize for any inconvenience that this may cause the Commission's Staff. However, the issues raised by Regulation D are numerous, complex and worthy of substantial discussion. My work schedule has not permitted me to prepare comments of this length within the time allotted. I hope that the Commission's Staff will nevertheless have an opportunity to consider my views inasmuch as it is my understanding that other commentators also have encountered delays in meeting the original deadline for comments.

<u>Introductory</u>

In my opinion, proposed Regulation D and the exemptive rules thereunder, if adopted, will provide a more understandable and coordinated (but not a less costly) exemptive framework for limited offering transactions particularly as they relate to the capital formation needs of small business. I congratulate the Commission and its Staff on what I consider both a refreshing and imaginative approach to revision and coordination of the exemptive provisions of Rules 240, 242 and 146, including especially the elimination of offeree qualification standards.

Nevertheless, I believe that there are several significant overall problems and numerous specific problems raised by the Commission's proposals. In my comments below, which are arranged based upon a provision-by-provision analysis of the Regulation, I have attempted to illustrate these problems. As a private securities practitioner whose principal involvement with the 1933 Act exemptive process has involved tax sheltered programs sold pursuant to Section 4(2) and Rule 146 exemptions, I address specifically certain portions of the proposals which I believe the Commission's Staff has drafted (probably inadvertently) in a manner which fails to achieve "tax neutrality." I urge the Commission and its Staff to give more thorough consideration to how all of the Regulation D proposals would affect partnership or other tax sheltered offerings whose unique characteristics are often overlooked in Commission rulemaking. In my view, some of the greatest problems presented by current Rule 146 arise in the tax sheltered area and are deserving of more thorough consideration because the volume of tax sheltered offerings which are made in reliance upon Rule 146 and Section 4(2), and are likely to be made under Regulation D, may well exceed the volume of any other types of offerings made in reliance on these rules with the possible exception of private placements of debt securities with institutions. The latter are not a regulatory problem.

SPECIFIC COMMENTS

Preliminary Note 4

The last sentence of this note should be reconsidered in light of the "accredited investor" concept that has now been recognized by statute and regulation. I am in agreement that proposed Rules 504, 505 and 506 should be issuer transactional exemptions. I am also in agreement that, with the exception provided in paragraph (a) of proposed Rule 504, the securities issued pursuant to these transactional exemptions should be "restricted" so that they cannot be resold to non-accredited investors without registration or availability of another exemption under the 1933 Act. However, why should an accredited investor be restricted from reselling securities to another accredited investor?

Now that the Commission appears willing to recognize that an unspecified number of accredited investors may participate in a Rule 505 or 506 offering, there is no sound policy reason for the Commission to be concerned about transfers of securities among accredited investors. Indeed, in the interest of promoting capital formation and liquidity, perhaps the Commission should be taking steps which would facilitate a secondary market among accredited investors in "restricted securities."

I dare say that this is a subject that may not have been contemplated within the primary focus of Regulation D; however, I feel that it is an issue which the Commission should consider rather than restating Preliminary Note 4.

Rule 501 - Accredited Investor Definition

Conceptually, I believe that it would be a sounder approach for the Commission to maintain a more substantial distinction between the concepts of "accredited investor" and "excluded purchaser." I believe that the persons defined in Rule 501(a)(5), (6) and (7) should fall within the category of excluded purchasers instead of accredited investors. Where this distinction really makes a difference is in the area of informational disclosure requirements and purchaser sophistication and representation requirements.

As the Commission proposes to structure Rules 505 and 506, if an offering is made entirely to accredited investors, Rule 502(b)(1)(i) does not require specific information to be furnished to purchasers. The problems inherent in this approach are perhaps best illustrated by the hypothetical situation where a tax sheltered offering might be made entirely to (a)(5)-(7) type accredited investors who are wealthy individuals, a very realistic possibility. In my view, not requiring informational disclosure under such circumstances is a mistake. Tax sheltered offerings are complicated. They are not the type of offerings that can be explained briefly, orally or often without the aid of competent professional advisers such as accountants, lawyers or financial planners. Broker-dealer involvement may be helpful but may also be a problem, especially if there is no written disclosure document. Many registered representatives do not understand tax shelters and will merely repeat whatever they are told to earn a substantial commission on a tax shelter. Also, in these types of transactions (as well as in many other offerings), disclosure of material risks and other aspects of the offering often are not focused upon by the issuer until the difficulties of describing the transaction are encountered by the draftsmen who have the burden of explaining it in writing.

Without a disclosure document, I also question the viability of the antifraud provisions of the federal securities laws to protect (a)(5)-(7) investors. I am not so naive as to suggest that most investors even attempt to read offering materials which are often well over 100 pages in length. However, their advisers may read these materials and the existence of the materials themselves acts as a deterrent to fraud, misrepresentation or non-disclosure. Moreover, the fact that an offering memorandum is in existence gives an investor a reference point for performance assessment and appropriate action in the event that the benefits of a proposed tax shelter or other offering terms prove to be materially different than represented.

My views above are not limited to the tax shelter area but are perhaps best illustrated by the problems in that area. Similar problems could arise with respect to any new venture financing.

On the other hand, I am sympathetic to the argument that much of the disclosure that would be required in a tax shelter private offering memorandum, by reference to the informational standards under Rule 146 and proposed Rule 506, is not necessarily the most relevant type of information for the tax shelter investor. However, the fault here lies in the fact that the Commission's existing registration forms, guidelines, etc., are not adequately "fine tuned" to the increasing number and variety of tax shelter offerings which are required to adhere to these requirements. (Recent improvements in Registration Guide 60 for real estate are a exception to this observation.) Thus, I feel that the Commission should retain a informational disclosure requirement for (a)(5)-(7) investors and focus instead upon improving and making more flexible and less burdensome the informational disclosure requirements for tax shelter and other types of issuers under the proposed exemptions.

For reasons set forth below, I consider unrealistic the Commission's proposal not to require informational disclosures to some non-accredited investors if an offering has at least 60% accredited investors.

Rule 501(a)(4) -- Directors and Officers of Issuers

It is unclear whether the term "executive officer" as used hereunder and as defined in Rule 501(f) includes within the reference to a "person who performs similar policymaking functions for the issuer" such persons as general partners of partnership issuers. A substantial number of unregistered offerings are made in partnership form and it would lend clarity to the Regulation if specific reference is made to the partnership situation, making it clear that general partners who will perform managerial or policymaking functions with partnership issuers are within the definition of "executive officer," and within Rule 501(a)(4).

Rule 501(a)(5)

This type of "accredited investor" appears to be a compromise between the $150,000 or more excluded purchaser under Rule 146(g) and the accredited investor who purchases $100,000 or more during a 60-day period under current Rule 242.

The Commission's objective should be to strike a balance between the objective of assuring that a purchaser of a large dollar amount of securities is per se able to fend for himself and need not be counted against the number of purchaser limits in proposed Rules 505 and 506, and the desirability of greater flexibility in unregistered offerings by permitting extended payment terms. In my view, the Commission's current proposal is unnecessarily harsh and restrictive in several respects.

First, it is important to bear in mind that the Federal Reserve Board margin rules and extension of credit prohibitions of the 1933 Act prevent most subscription arrangements for registered offerings whereby an investor may pay a portion of the purchase price for securities over a period of years. [Footnote: In this connection, it is recommended that the Commission and its Staff coordinate with the Federal Reserve Board to assure that their existing interpretation to the effect that margin and extension of credit requirements do not apply to Section 4(2) offerings also will be the case with respect to Rule 506 and other Regulation D offerings.] By proposing an arbitrary two-year cutoff on amounts to be paid in installments by an (a)(5) type of accredited investor, the Commission is further adversely limiting some of the flexibility that non-public offerings have over public offerings. The economic structure of many non-public offerings, especially tax sheltered offerings, may contemplate an investment program spanning over several years.

My suggestion is to permit as an alternative to the $100,000, two-year requirement, any series of installment payments, the net present value of which, discounted at a universal interest rate benchmark such as the federal funds rate, prevailing at the commencement of the offering, would equal at least $100,000. For example, this would permit, in most economic circumstances, installment purchases of $150,000 over a three year period and $200,000 over a four year period to come within the Rule 501(a)(5) definition. Under this approach, most installment type offerings would be accommodated, while, at the same time, not diminishing the amount of an investor's personal liability below $100,000 on a net present value basis.

Proposed Rule 501(a)(5) also is the first specific illustration of my general comment that Regulation D as drafted is not "tax neutral." Specifically, the Commission's proposal that an unconditional obligation to be discharged within two years must be secured by an unconditional letter of credit, is an unduly narrow limitation, the purpose of which is unclear, but the consequence of which is clearly disadvantageous to investors. The Tax Reform Act of 1976 ("1976 Act") was adopted to proscribe certain practices whereby investors in tax sheltered offerings were previously able to claim tax deductions substantially in excess of their actual investment at risk in such offerings. However, the 1976 Act contains provisions which permit deductions in excess of an investor's cash investment provided the investor is "at risk" with respect to additional amounts so that the amount of deductions claimed do not exceed the amount "at risk." Letter of credit arrangements are only one manner in which an offering may be structured so an investor may satisfy these at risk requirements. Others include arrangements whereby an investor may pledge collateral other than his interest in the offering, in order to achieve "at risk" status. Also, it is possible under the 1976 Act for an investor to be at risk with respect to a full recourse promissory note even if such note is not secured by a letter of credit or pledge of other collateral if the investor assumes a pro rata portion of underlying indebtedness to the issuer (usually a limited partnership), limiting such assumption to the principal amount of the investor's promissory note(s).

The effect of the Commission's proposal to require an unconditional letter of credit effectively discriminates with respect to tax shelter offerings in favor of one at risk mechanism to the exclusion of other legitimate at risk mechanisms. There is no securities-related reason why the Commission's proposal should be limited to a letter of credit requirement. [Footnote: In this connection, the term "unconditional" as used in connection with letter of credit appears inaccurate. Most letters of credit are conditional at least in the sense that they are drawn down only upon the failure of a condition (e.g., payment of an investor's note). The proper reference should be "irrevocable letter of credit."] Moreover, letter of credit arrangements are often not beneficial to the capital formation process or individual investors because they restrict liquidity. Obtaining letters of credit can be costly and unduly burdensome, especially where an issuer having no reason to be concerned about a purchaser's credit standing, would not require a letter of credit.

<u>Rule 501(a)(6)</u>

There is certainly room for reasonable disagreement as to what is a proper Rule 501(a)(6) net worth amount in an absolute sense and relative to the income test in proposed Rule 501(a)(7). The North American Securities Administrators Association ("NASAA") has adopted suitability guidelines for several types of tax sheltered offerings. These currently provide for a $225,000 net worth requirement (exclusive of home furnishings or automobiles) or $60,000 of net worth (with the same exclusions) and $60,000 taxable income. Assuming these alternative economic tests are reasonably related, as I believe they are, it seems to me that the Commission's proposed $750,000 net worth standard is unduly high compared to the $100,000 adjusted gross income test in proposed Rule 501(a)(7). Also, regardless of what figure the Commission uses in Rule 501(a)(6), it may wish to make an exclusion for home, furnishings and automobiles, if, as it appears, the objective is to assure that an accredited investor has substantial liquid net worth at his disposal. My recommendation is a $750,000 test excluding the aforementioned items.

As drafted, the Commission's proposal also leaves many unanswered questions. To resolve two of these, I recommend that the Commission clarify that the net worth test is based upon fair market value as represented by the purchaser and, where a joint investment is being made with a spouse, such net worth may include the net worth of the spouse.

Rule 501(a)(7)

It is a serious mistake to use an adjusted gross income standard for purposes of this provision. The problem is most apparent again with respect to tax sheltered type investments because most of these will be in partnership form and losses generated during the early (shelter) years of a partnership are treated as a deduction in arriving at an individual limited partner's adjusted gross income. Thus, under the Commission's proposal, many individuals may have gross income substantially in excess of $100,000 but because of sound and lawful tax planning, they may have reduced their adjusted gross income to substantially smaller amounts. Since these individuals will very often be the types of investors who should be considered accredited investors (or preferably, excluded purchasers) for purposes of tax shelter or other unregistered offerings, the Commission's proposal to use an adjusted gross income test is another example of lack of tax neutrality. The real objective should be to obtain some assurance that an individual has substantial liquidity. Gross income from all sources is the better measure of such liquidity. My recommendation is to provide that $100,000 or perhaps $125,000 of gross income from any source is sufficient for purposes of the proposed Rule 501(a)(7) test.

Rule 501(a)(7) proposal also is deficient in that the Rule requires that the income must be reported for federal income tax purposes. In my experience, there have been not infrequent examples where persons may not have to report $100,000 of income for federal income tax purposes but clearly have income amounts substantially in excess of this level. Two obvious illustrations are investors who have substantial amounts of tax exempt interest income and aliens who are not required to file a U.S. tax return or report all of their income on a U.S. return. Again, I recommend that the Commission rephrase the test in terms of gross income from all sources.

Finally, I have learned that the Commission and/or the NASAA states are considering requiring that the income threshold of the Rule 501(a)(7) be met for more than one year. I do not feel that any useful purpose would be served by such a modification. In our current economic environment, incomes change rapidly. The fact that individuals may have $100,000 of income only during the past year as opposed to the two last years probably has no bearing upon the individual's investment sophistication or his current liquidity. Also, there may be legitimate situations in the tax sheltered area where an individual has a substantial amount of nonrecurring income which the individual may quite properly wish to shelter by a tax sheltered investment. What the individual's income was two years ago is wholly irrelevant for such purposes. My recommendation is to rephrase proposed Rule 501(a)(7) with a provision which indicates that the individual must have during the most recent calendar year or expect to have during the current calendar year the requisite amount of gross income from all sources. Finally, a spouse's income should be included for purposes of Rule 501(a)(7) in circumstances where an investment is being made jointly by an individual and his spouse.

Rule 501(d) -- Calculation of number of purchasers

As noted in my comments above, I believe that Regulation D would be on conceptually sounder footing, reconciling investor protection and capital formation concerns, if the categories of accredited investors presently set forth in proposed Rule 501(a)(5)-(7) were treated instead as excluded purchasers. As the Commission proposes, an issuer would then have to satisfy all other applicable provisions of Regulation D, including informational requirements, with respect to excluded purchasers.

Both with respect to the concept of accredited investor and excluded purchaser, regardless of which persons go into which category, the Commission should recognize that no one set of objective definitions will ever provide 100% assurance,, for example, that an accredited investor is able to fend for himself. However, the Commission will be on much safer grounds in permitting a larger number of purchasers to be treated as excluded purchasers subject to informational safeguards of Regulation D, than by expanding the class of "accredited investors" to include persons who may, in fact, need other protections afforded by the Regulation. Regardless of how the Commission reconciles this issue, I believe that the Commission's attempt to expand while at the same time lending some objectivity to these categories, is commendable.

One further constructive step that the Commission should take to improve Regulation D would be to add an additional, subjectively defined category of accredited investor under Rule 501(a). This category should be the "access investor," a concept that the Commission apparently proposes to delete from Rule 506, notwithstanding the substantial precedent under Rule 146 and prior Section 4(2) case law, recognizing that "access investors" need not receive informational disclosure documents. I do not think that it is prudent or appropriate for the Commission to now abandon this concept on the rationale that the question of who is an access investor is solved merely by objectively defining certain persons as "accredited investors." No set of objective definitions will satisfactorily resolve in all situations what is an inherently subjective determination. For these reasons, I recommend that the Commission add to Rule 501(a) an additional category of "access investor" using the criteria set forth in current Rule 146(e) as a guideline. This modification, in my opinion, would lend additional flexibility to the Rule and would go a long way toward avoiding what may be a continuing debate as to the appropriate categories of persons who should be treated as accredited investors or excluded purchasers.

Rule 501(h) -- Predecessor

Use of the "predecessor" concept may result in some inequitable results in cases, for example, where a large company has acquired an unaffiliated small company, yet the small company's prior activities in connection with securities offerings may render Regulation D unavailable with respect to one or more proposed securities offerings by the large company. The Commission's concern in specifying how to calculate offering limitations could be alleviated by use of the already defined term, "affiliate."

Rule 501(i) -- Purchaser Representative

One of the most pleasing aspects of proposed Regulation D is the Commission's recognition that the focus on qualifications of investors and investor representatives should be upon purchasers and purchaser representatives rather than offerees and offeree representatives. I support this approach wholeheartedly. Nevertheless, there are still some unnecessary vestiges of Rule 146 which remain in the definition of purchaser representative. For example, I do not believe that it is sound to provide that a purchaser representative may not be an affiliate, director, officer or other employee of the issuer or beneficial owner of more than 10% of the issuer's securities. A conceptually simpler approach would be to permit each purchaser to chose his own representative. Disclosure of such affiliation and compensation interest to a purchaser should be the only necessary safeguard in these circumstances. Indeed, I can visualize many circumstances where a purchaser would be more comfortable with a person falling within the now precluded categories as his offeree representative with respect to an issuer's offering than with an outside representative such as a broker-dealer firm's account executive who may have less knowledge and information concerning the issuer.

If the Commission does not accept my view in this respect, I feel that in any event that the exclusions now set forth in Rule 501(i)(l), (ii) and (iii) should be modified so that they conform with the provisions concerning trusts or estates, corporations, etc., now set forth in Rule 501(d) regarding exclusions from the number of purchaser limitations. There is no reason to use these provisions differently within the same regulation.

Rule 501(i) also illustrates the first appearance in proposed Regulation D of what I consider the benevolent myth of broker-dealer (and in this case, investment adviser) regulation. In effect, the Commission is warning individuals who may act as purchaser representatives (formerly, offeree representatives) that if they do so, they may be subject to registration as broker-dealers or investment advisers, and, thus, to a comprehensive scheme of regulations applicable to such persons under the federal securities laws. In my view, the Commission should delete Note

1 to Rule 501(i). The Note, in my opinion, leads to a result which is exactly contrary to the policy which the Commission should be attempting to foster with respect to Regulation D, i.e. , assuring that purchasers who need professional representation, receive such representation in the most effective and reasonable fashion.

In my experience with Rule 146, including the execution of Form 146, many banks, attorneys, accounting firms, etc., although they have assisted purchasers in connection with an offering, will go to great lengths in insisting that they are not offeree representatives because of their concern about broker-dealer and investment adviser regulations being applied to them. On the other hand, if a purchaser needing a representative cannot find a qualified attorney, accountant or financial planner to represent him in connection with an offering because such person is concerned about being labeled a broker-dealer or investment adviser, then the purchaser may be forced to turn to persons falling within the category of registered investment advisers and broker-dealers. The Commission and its Staff should consider the realities of what happens under these circumstances. The most likely scenario is that the broker-dealer or investment adviser is the one involved in offering the securities on behalf of the issuer and, therefore, will receive a commission. Under such circumstances, it is, in my view, somewhat unrealistic to believe that many broker-dealers or investment advisers will act independently in the best interests of the purchaser.

Finally, perhaps the most offensive part of Note 1 is the implicit reasoning that only broker-dealers and investment advisers who are registered, may be in the best position to represent and advise purchasers. Considering the minimal overall qualification standards of the registered representative component of the broker-dealer community, and the substantial number of supervision and enforcement problems that have been encountered by state, NASD and Commission personnel in regulating these "registered professionals," the Commission should seriously reevaluate what useful purpose is served by suggesting that purchaser representatives may have to be registered broker-dealers or investment advisers. If the Commission is concerned that registration of these persons gives the Commission a supervisory "handle" over them, this "handle" is probably no more useful than the ability which the Commission already would possess to enjoin individuals whose purchaser representative activities were of such a magnitude as to require them to register as broker-dealers. Moreover, the fact that individual broker-dealers and investment advisers may be subject to Commission or self-regulatory agency disciplinary actions for acting improperly as a purchaser representative, is unlikely to serve as a preventive safeguard from the point of view of the purchasers who were represented.

Here again, my most serious concerns are in the tax shelter area where I feel that many broker-dealers are not capable of advising purchasers adequately concerning tax shelter investments. For these reasons, I recommend that Note 1 be deleted. It would be more appropriate to clarify in a note that the fact that a person is associated with a registered broker-dealer does not automatically constitute such person a qualified purchaser representative with respect to all offerings.

Rule 501(j) -- Securities of the issuer

As noted above, the use of the "predecessor" concept in subsection (2) of this definition may result in unintended aggregation of securities issues where such aggregation is clearly inappropriate.

Rule 502(a) -- Integration

While the six months "safe harbor" which the Commission proposes herein may be a workable guideline in the circumstances of a small corporate enterprise progressing through its initial financing stages toward the time that it goes public, the safe harbor is of very little utility in the area of tax shelter offerings. Very often, these type offerings involve installment payments or additional assessments which make it impossible for an issuer to establish a "clean" six month period between offerings even though the tax shelter syndications clearly involve different underlying investments which should not be deemed integrated.

Release No. 4552 also is too vague and ambiguous to assist issuers and their counsel in determining whether offerings must be integrated. For these reasons, I urge the Commission to consider adoption of a new interpretive release concerning integration of offerings. In my view, primary emphasis needs to be placed upon the fact that offerings should be integrated unless they involve substantially the same underlying investment risks.

One specific comment concerning Rule 502(a) as proposed, is that the reference to Rule 16b-3 of the Securities Exchange Act for purposes of defining the employee plan exclusions is too restrictive and has no place in Regulation D. Many of the smaller issuers who will be utilizing Regulation D either will not have an employee plan approved by stockholders or, indeed, may not have the ability to meet other conditions of the Rule such as administration of a stock option plan by three disinterested persons. Insofar as Rule 16b-3 embodies these "corporate governance" type conditions, its use is inappropriate in connection with Regulation D.

Rule 502(b)(1) -- Information Requirement - 60% Test

I do not believe that the 60% test is workable and I recommend that it be deleted from Regulation D.

The ability of the institutional type accredited investors and individual accredited investors to evaluate information will differ markedly. Generally, institutional investors will have an advantage because of professional staffs and they may receive information which would not be understandable by an individual non-accredited investor even if he asked for such information.

Second, the fact that more than 60% of the offering is being sold to institutional investors does not really reduce risk for individual non- accredited investors. Suppose, for example, that a financial institution with over $1 billion of investment assets is committing $200,000 to an offering while a non- accredited investor with total assets of $500,000 is committing $50,000 to the offering. Under these circumstances, as a matter of modern portfolio theory and common sense, satisfaction of the 60% test regardless of what informational material may or may not be available, will not improve the lesser ability of the non-accredited investor to bear the risk of loss.

Third, it is not clear how the 60% test can be implemented in practice. The Commission appears to visualize that it can be determined in advance whether more than 60% of an offering will involve institutional-type accredited investors.

Finally, even if a situation were properly structured so that a non- accredited investor might simply ask to see the same written information provided to institutional participants, it is unlikely as a practical matter that this requirement of the Rule would be observed. Consider, for example, whether persons purchasing a registered offering of securities now receive the same type of information made available to banks and underwriters. Consider what would happen if a prospective investor in such an offering were to request such information from a participating underwriter. In all probability, he would be excluded from the offering. This equivalency of information problem also exists with respect to the dichotomy between investment research made available to individual investors and to institutional investors. The chances of an individual non-accredited investor receiving the same type of written information that is provided to an institutional investor in a Regulation D offering are about the same as the chances of a prospective purchaser of 100 shares of IBM receiving the same type of institutional research provided by his broker to a $1 billion pension fund investor. It doesn't happen.

I offer one technical comment if the Commission decides to retain the 60% test. The qualification of the term "non-accredited investors" by use of the word "individual" is potentially confusing. Is the Commission suggesting that there are corporate or other entity type non-accredited investors who are to be treated differently than individuals? Also, as drafted, the Commission's proposal could result in the anomalous situation where a non-accredited investor has a right to request and receive information provided to institutional-type accredited investors while there may be Rule 501(a)(5)-(7) type individual accredited investors (or possibly some institutional accredited investors) who, by virtue of Rule 502(b)(1)(i) would not be entitled to, and may not in fact, receive any informational disclosure notwithstanding the fact that some institutional-type accredited investors receive such information. This possibility lends further support to my overall comment that Rule 501(a)(5)-(7) accredited investors either should be subject to informational disclosure requirements or, more preferably, should be included within the category of excluded purchasers.

Rule 502 (b)(2) -- Type of information to be furnished

The approach taken by the Commission under proposed Rule 502(b)(2)(i) is to attempt to gear informational disclosures to the size of an offering and whether an issuer is a reporting company. - As a practicable matter, J doubt that such an approach will have much effect in the case of non-reporting companies since most securities counsel will base disclosures made in a disclosure document upon a relatively stringent evaluation of what material information is required to be disclosed. In this respect, the Commission's disclosure forms, guides, etc., are, and will also remain, at best minimal indicia of some of the types of informational that are material.

What is unfortunate with respect to the Commission's approach is that often items of information in Commission forms, guides, etc., are clearly immaterial to the circumstances of a particular unregistered offering but securities counsel, by virtue of current Rule 146 and the Commission's Regulation D proposals, would feel constrained to observe the literal requirements of the form. For example, neither Regulation A or Forms S-1 or S-18 are particularly well suited to non-corporate type offerings, including tax shelter offerings.

Also, the Commission's existing Rule 146 and proposed Regulation D adopt a disclosure standard for unregistered offerings which is essentially identical to the disclosure requirements for registered offerings. It is not clear from the Ralston Purina case or its progeny that so stringent a disclosure requirement is mandated by Section 4(2). It is my view that the informational standards should be stated in terms of purchasers receiving substantially the same kind of information that would be required to be included in a registered public offering to the extent that such information is material to an investment decision with respect to the unregistered offering. In this connection, I question whether it is useful or necessary to provide specific reference to disclosure forms for different size offerings. In my view, the Rule should indicate that informational disclosure shall be substantially equivalent to information that the issuer would be required to disclose under the available registration form under the 1933 Act or Regulation A (to the extent the offering is within the dollar limits), and to the extent that any such information is material to an investment decision with respect to the unregistered offering.

Audited Financial Statement Requirement

The introduction of audited financial statement requirements in Regulation D, in my view, is a step backward in terms of reducing capital formation burdens and costs. Also, the requirements as phrased are unnecessarily confusing. The Commission should recognize that there are many offerings where audited financial statements are not relevant or material to investors in connection with the offering. These include start-up situations where there has been an incorporation but no substantial assets have yet to be contributed to the issuer.

There are also numerous tax sheltered offerings in non-corporate form currently made in reliance upon Rule 146. In these cases, the non-corporate entity, usually a limited partnership, either has not been formed or has been formed with a nominal limited partner (perhaps a contribution of $100 or $1,000). Under these circumstances an audited financial statement of the limited partnership is an unnecessary requirement. Moreover, to require an audited balance sheet with respect to a general partner, based upon the rationale now used for registered public offerings that some disclosure of the general partner's financial condition may be relevant to investors in indicating the general partner's ability to perform its obligations under the partnership agreement, etc., may work hardships in connection with smaller unregistered offerings. Often, there is only a nominal corporate general partner or no corporate general partners, but there are individual general partners whose presence is required in order to sustain a favorable tax ruling or opinion of counsel as to partnership classification for federal income tax purposes. Where there is no corporate general partner, proposed Regulation D should make clear that individual financial statements will not be required. All that should be required to provide an assurance of a general partner's financial condition is a written representation made in the offering document and subject to the liability provisions of the federal securities laws, that the general partner(s) have a net worth of x amount or over x amount.

There are also many advantages of timing in connection with non-public offerings which will be rendered unavailable if the Commission insists upon audited financial statements because there will be a delay in preparing such statements. Many non-public offerings are made because an issuer and its representatives have made a decision to avoid the delay and expense involved in connection with a registered offering, including audited financial statements. The Commission's current proposals would clearly detract from this much needed flexibility. Also, the Commission's proposals as drafted are unclear as to how timely financial or unaudited financial statements would have to be under various circumstances.

It is my understanding that several of the NASAA states with whom the Commission seeks to coordinate the adoption of Regulation D feel strongly that audited financial statements are an essential requirement. However, it does not follow that such a requirement should be included in Regulation D at the federal level thereby becoming a universal disclosure requirement for offerings made in all jurisdictions. Historically, issuers and their securities counsel have had to live with individual state policies requiring audited financial statements. Why not leave the audited financial statement requirement out of Regulation D as a matter to be required by individual states in their discretion? An issuer would then have the flexibility of electing to avoid making offerings in certain states where audited financial statements are required and their preparation would be prohibitively expensive. Historically audited financial statements have not been required for certain Regulation A offerings or other exempt offerings. No sound arguments have been advanced by the Commission as to why a change in policy is required.

My recommendation is that the Commission not require audited financial statements except with respect to those issuers who have previously prepared audited financial statements, and then only where the issuer believes that such financial statements are material to an investment decision with respect to the offering, I recommend that the Commission specifically address the problem of financial statements for non-corporate offerings and that only an unaudited balance sheet for any corporate general partners should be required in such offerings, unless the corporate general partner has previously prepared audited financial statements.

<u>Rule 502(b)(2)(iv) -- Opportunity to ask questions</u>

In my view, the opportunity to ask questions in connection with any unregistered, or for that matter registered, offering is an important safeguard especially under the circumstances of proposed Regulation D which now envisions circumstances where there will be no specific informational disclosure requirements. I recommend that this requirement also be made applicable to Rule 504 offerings.

<u>Rule 502(b)(2)(v)</u>

As noted in my comments above, I feel that this provision should be modified to eliminate the 60% test and to allow for the fact that the categories of persons now set forth in Rule 501(a)(5)-(7) should receive informational disclosures.

<u>Rule 502(c) -- Limitation on manner of offering</u>

The synopsis in Release 33-6339 indicates that this provision is similar to the provision contained in Rule 146(c) except that the prohibition against seminars and meetings has been modified to reflect the elimination of the qualified offeree concept of Rule 146. However, an examination of the wording of Rule 502(c)(2) indicates that, while somewhat ambiguous, the permissible range of offering activities may now have been materially limited by the Commission through the use and the placement in this subparagraph of the words "mailing," "advertising" and "notice." Rule 146(c)(1) includes two of these terms, but excludes the term "mailing." Moreover, as used in Rule 146(c)(1), the terms "advertisement" and "notice" appear to be qualified by the requirement of publication in any newspaper or other media defined therein. It is not clear from the wording of proposed Rule 502(c)(2) that the words "advertisement" and "notice" are so qualified. This is especially true since these words appear in the same phrase as the word "mailing." The concept of a mailing being published in any of the media described in paragraph (c)(1) is difficult to comprehend and not consistent with the normal understanding of this term. These three terms do not appear at all in current Rule 240 and the term "mailing" does not appear in the counterpart provision of Rule 242.

In my view, a mailing which does not violate the overall prohibition of Rule 502 (c) with respect to general solicitation or general advertising, should not be prohibited under Regulation D. There is no sound reason to prohibit a mailing, or for that matter a notice which may be directed to prospective purchasers inviting them to attend a seminar or meeting concerning the offering. In this respect, the Commission's proposed language in Rule 502 (c)(2) may be construed as an attempt to introduce some form of "gunjumping" prohibition into the unregistered offering process. One of the salient advantages of the exemptive process, both from the standpoint of investors and issuers and their representatives is that "the rigidity of the three different offering periods under Section 5 of the 1933 Act is not governing with respect to what can and cannot be done during various time periods.

In the circumstances of a Regulation D offering, especially under the circumstances proposed by the Commission where all investors may not be receiving written disclosure, it would appear to further the Commission's objectives to permit mailings to a limited number of prospective purchasers inviting such persons to attend a seminar or meeting. Mailings for other purposes, such as advising persons of the existence of the offering and allowing them to fill out a questionnaire or other document if they wish to receive offering materials, now clearly appear to be permitted under Rule 502(c)(1), as they should be, subject to the overall prohibition on general solicitation or general advertising. Therefore, the proposal to adapt a special rule with respect to a seminar or meeting invitation is unclear and appears unwarranted. It is my recommendation that the term "mailing" be deleted from this provision and that if the terms "advertisement" and "notice" are retained, it should be made clear that in the context which they are used, they are intended to prohibit an advertisement or notice in the media described in paragraph (c)(1) of Rule 502(c) which would constitute general solicitation or general advertising.

Rule 502(e) -- Remuneration paid for solicitation or sales

A most serious shortcoming of Regulation D is the proposal to add a requirement Which would impose this additional condition and substantial burden upon offerings made under the Regulation D exemptions. In the synopsis of this provision in Release No. 6339, the Commission asserts that it does not believe that the additional requirement will add any burdens to the issuer since in most instances persons soliciting prospective buyers or selling the securities of the issuer would be subject to broker-dealer registration provisions under applicable state and federal laws. I believe that this statement is both incorrect as a factual matter with respect to additional burdens placed upon issuers and as a legal matter with respect to the conclusion that in most instances, persons soliciting prospective buyers or selling the securities of the issuer will be subject to broker-dealer registration, at least at state levels.

First, the Commission's proposal will clearly place additional capital formation burdens upon issuers seeking to make unregistered securities offerings under Regulation D because it will force any issuers who are not in a position to sell securities without paying commissions or similar remuneration to have to deal with a limited class of registered broker-dealers to the exclusion of other persons who might assist the issuer in offering its securities, including finders, business consultants, business brokers or promoters, and the issuer's own officers, directors and employees. Also, the Commission appears to ignore intrastate broker-dealers. The effect of the Commission's proposal would be to require their registration under federal laws if they are to participate in an unregistered Regulation D offering. It should be evident to the Commission and its Staff that if they restrict the number of persons who are eligible to handle an offering by a regulatory requirement, they put those persons in a position to charge more for their services. The new issue market is a classic example of this phenomenon notwithstanding the fact that this is a market (unlike non-public offerings) where underwriting compensation is monitored as to fairness by NASD. Nevertheless, the effect of such monitoring is to have commissions on virtually all underwritten offerings for new issues rise to the permissible maximum under NASD's corporate finance guidelines. How many examples has one seen of an underwriter of a new issuer receiving warrants or options to purchase less than 10% of an issue, or an underwriter who charges an underwriting commission of 5% instead of 8-10%? It rarely happens.

An even more serious effect of the Commission's proposal is the fact that many issuers, for one reason or another, may not have realistic access to the registered broker-dealer community. If such issuers may not sell their securities without paying some compensation to other persons, then the effect of the Commission's proposal is to foreclose these issuers from utilization of Regulation D. The effect is just the opposite of the Commission's intended objectives under Regulation D, to facilitate capital formation by small issuers.

Also, I believe that the Commission's assertion that broker-dealer registration would normally be required under applicable state laws with respect to involvement in Regulation D type offerings is incorrect in most circumstances. Most states securities laws now provide exemptions from broker-dealer or agent licensing provisions of their securities acts if the securities transaction involved involves a limited number of persons offering or is an exempt transaction under the state statute.

The Commission states in Release No. 33-6339 that it "believes that the requirement with respect to broker-dealers will provide safeguards for investor protection since a registered broker-dealer, pursuant to its suitability obligations, must make a determination as to whether participation in the offering is appropriate for each investor." While this observation concerning suitability may be correct, it raises some very interesting questions concerning the responsibilities of issuers and others under Regulation D and existing transactional exemptions. Is the Commission suggesting, for example, that issuers do not have substantially equivalent responsibilities under the antifraud provisions of the federal securities laws? If so, perhaps the Commission should make a statement to this effect or clarify what responsibilities, if any, it believes that issuers and their non-broker dealer representatives have with respect to investor suitability determinations in exempt offerings under Regulation D. For example, what is the purpose of the rather comprehensive offeree qualification and offeree representative requirements, including the sophistication and economic risk provisions now found in Rule 146? Are they not in effect suitability determinations? Also, what is the nature of the purchaser qualification and purchaser representative tests now found in Regulation D? Are they not a form of investor suitability determinations? Isn't the doctrine of a broker-dealer investor suitability responsibilities based on the antifraud provisions of the federal securities laws which are applicable to all persons, not just broker-dealers? Isn't the broker-dealer suitability doctrine merely a specific manifestation of antifraud concerns with respect to suitability that arise most frequently within the broker-dealer community? Finally, why is it realistic to believe that a broker-dealer will exercise investor suitability responsibilities to a greater degree than an issuer when the broker-dealer's principal interest in a transaction is its ability to earn a commission, while an issuer raising funds from such individuals will have ongoing obligations to such persons as security holders under state and possibly federal law.

Regardless of what the Commission's view may be as to an issuer's responsibilities, it should be noted that the NASAA states have taken the position through real estate, oil and gas and other guidelines that there are investor suitability obligations placed upon the issuers of securities to make sure that the purchasers are in fact suitable in terms of net worth, taxable income and related criteria. Thus, one is constrained to ask what the Commission feels is added in terms of investor suitability by broker-dealer involvement.

I appreciate that there are some NASAA states with whom the Commission proposes to develop a coordinated Regulation D exemption, who feel strongly that if commissions or similar remuneration are paid in connection with the offering, there should be broker-dealer registration. However, as noted above, there are other states who do not currently require such registration for exempt transactions. It is my recommendation that the Commission delete the registered broker-dealer requirement from Regulation D leaving this matter to the individual states. Under the approach, many Regulation D offerings would not be burdened by broker-dealer impediments.

I also offer one technical criticism of proposed Rule 502(e). As drafted, this provision literally indicates that if commissions are paid, the broker-dealers involved would have to be registered in all states in which the securities are offered. I hope this result was unintended.

As a final commentary on the broker-dealer/commissions-remuneration issue, I think the Commission should take into consideration the fact that if Rule 502(e) were adopted as a part of Regulation D, the Commission's Staff is likely to be flooded with questions as to what constitutes commissions or remuneration in connection with an offering. For example, if an issuer uses a finder to place securities in an offering and pays no commissions or other cash remuneration to the finder but gives the finder options, warrants or cheap stock, is this remuneration? What about a right of first refusal? The Commission should be aware that some states have asserted in their securities laws, which contain language substantially identical to proposed Rule 502(e) concerning payment of commissions or similar remuneration, have been interpreted by the courts, to render non-public offering exemptions unavailable at the state level where, for example, funds were paid to the promoter or general partner of a tax sheltered offering. See, e.g., Petroleum Resource Development Corp. v. Day, 585 P.2d 346 (Okla. 1978) (offering proceeds retained by issuer in excess of direct and indirect costs of oil and gas exploration project held to constitute a form of indirect remuneration rendering limited offering exemption unable); Upton v. Trinidad Petroleum Corp., U.S.D.C. N.D., Ala. S.D. (Mar. 26, 1979) CCH Blue

Sky L. Rep. ¶ 71,474 (limited offering exemption predicated upon non-payment of commission or other remuneration is not available where issuer received money in excess of actual cost of turnkey drilling contracts sold to investors); Schultz v. Rector-Phillips-Morris, Inc., 552 S.W.2d 4 (Ark. 1977) (consulting fees held to constitute remuneration rendering private offering exemption unavailable); and State ex rel Day v. Petco Oil & Gas, Inc., 558 P.2d 1163 (Okla. 1977) (additional supervisory fees in connection with oil and gas exploration constitute a form of indirect remuneration rendering limited offering exemption unavailable). As these cases illustrate, there may be a very fine line between legitimate offering proceeds or compensation to an issuer and commissions or other remuneration paid to persons who sell the securities. Such interpretative questions are likely to be substantial if Rule 502(e) is adopted. On the other hand, it is a well established fact that with respect to the multitude of non-public tax shelter the offerings, as is the case with registered tax sheltered offerings, it is net at all unusual for an issuer-general partner to receive a management fee, supervisory fee, or similar compensation in connection with the initial stages of a tax shelter syndication. By proposing to adopt Rule 502(e), think that the Commission will find that it and its Staff either will be faced with the possibility of either taking the draconian position that anything that is compensation to the issuer or its management in connection with a newly formed enterprise is a form of commission or similar remuneration, or they will be barraged with numerous questions concerning the distinction between offering compensation and management compensation. Neither of these prospects is very encouraging or helpful to the capital formation process. My recommendation is that the Commission not adopt Rule 502(e).

Rule 503 - Filing of notice of sales

It is my view that a notice should not be repaired at all. If required, a notice should not be a condition of availability of an exemption.

If a notice is required, I urge the commission to clarify what is meant by the first sale of securities. For example, is the receipt of subscription funds held in a special bank or escrow account pending receipt of minimum subscriptions to enable an issuer to accept any subscriptions, considered a sale of securities before acceptance of the subscriptions is permitted under the offering conditions?

I am also opposed to the proposed undertaking requirement in Rule 503 which would require an issuer to furnish a copy of disclosure documents to the Commission or a state securities administrator upon request. There is an unfortunate tendency for undertakings to become absolutes. Also, I question whether the undertaking is necessary since, if the notice is required, a state or the SEC should be in a position to request, or failing a response to such request, to subpoena such information as it sees fit. Surely the undertaking is not considered an essential enforcement tool since the issuers most likely to violate Section of the 1933 Act are the issuers most likely not to file any notice with SEC or the states.

Rule 504

I am opposed to the denial of this exemption to companies subject to the reporting requirements of Section 13 or 15(d) of the Securities Exchange Act. Notwithstanding the fact that reporting companies should have less of a problem complying with informational disclosure under the Rule, there are still many circumstances whore a reporting company night see fit to utilize Rule 504, For example, employee, pension, profit sharing or similar plans involving an investment in securities of the issuer by an employee could be the type of offering that is best exempted under Rule 504 because of the employees' connection with the issuer and the employment related nature of such investments. In this connection, the type of information which the Commission no doubt envisions that a reporting issuer would have available for distribution to purchasers in the form of 10-K reports, annual reports proxy statements, etc., is not the type of information that is most critical with respect to employee plan type securities investments. Reporting issuers should not he forced to utilize Form S-8 or, if possible, a non-public offering exemption under Rule 506 for such type transactions. Rule 504 would lend additional, much needed, flexibility in this area. Also, there may be circumstances where a Rule 504 exemption may be available to a reporting issuer where for reasons of purchaser qualifications or other numerical limits, a Rule 506 exception might not be available.

I believe that the Commission should consider the possibility of allowing a higher offering threshold under Rule 504 with respect to offerings that are registered at the state level. If the limitation remains at $500,000 for state level registered Rule 504 transactions, the utility of the Rule is likely to be less because of the offering costs involved in state registration. Also, there is likely to be very little liquidity in any secondary market involving an offering limited to $500,000.

I believe that Rule 504(a) also contains a technical drafting error in that it makes Rules 502(c) and (d) inapplicable to Rule 504 offerings, which, are made exclusively in states which provide for the registration of such securities. The Commission should recognize that in addition to the few states that may exempt Rule 504 transactions (a few states now exempt Rule 240 transactions), and the states that will require registration of such transactions, there is still a third group of jurisdictions who may follow neither policy. New York is one example; the District of Columbia is another.

Insofar as Rule 504 transactions may result in freely transferable securities at the state level, I think that the Commission's proposal should clarify that such securities would be freely transferable within or among those states that either have allowed registration of the securities or provide an exemption from registration with respect to the initial issuance of the securities in the Rule 504 offering, or with respect to secondary transactions once such securities have been issued.

Rule 505

For reasons similar to those expressed with respect to my comments on Rule 504, believe that issuers who are reporting companies should be entitled to use Rule 505.

Without going into specifics, I feel that the "bad boy" provisions of Rule 505 should be re-examined to make sure that they do not result in unintended disqualifications.

Regulation A Exemption

The Commission suggests in Release No. 6339 that the Regulation A exemption will no longer be necessary in view of the relaxed registration provisions of Form S-18 and the proposal (issued subsequent to Release No. 6339) to reduce reporting burdens under the Securities Exchange Act for certain issuers. It is my view that rescission of Regulation A would be a mistake. First, I believe that most of the differences between a registered offering on Form S-18 and Form S-1 are more perceived by the Commission than practitioners. To the extent that there is some relaxation of registration disclosure requirements and reporting burdens, it is natural to expect that issuers will use the easier Form S-18 if they have to register in the first place. However, to suggest that the fact that they can register and may have some reduction in reporting burdens makes Regulation A unnecessary is, in my view, faulty reasoning. Regulation A affords an issuer an opportunity to sell up to $ 1,500,000 of securities. Until the close of the first fiscal year following such offering and until the issuer has more than $1 million of total assets or more than 500 holders of record of the class of equity securities, the issuer is not required to register under Section 12 of the Exchange Act and thereby avoids becoming subject to substantial periodic reporting, proxy solicitation and other requirements. To raise the possibility that these burdens may be relaxed in certain circumstances as a result of Form S-18 registration or the Commission's more recent proposals, is simply not the same thing as a Regulation A issuer having the choice of structuring an offering to avoid these requirements entirely. The Commission should retain Regulation A and afford issuers a choice as whether they wish to go public under the securities Exchange Act.

Rule 506

In the format included in Release No. 33-6339, proposed Rule 506 does not appear to constitute a statutory exemption. This result appears to be due to either drafting errors, printing errors or a combination of both, which I assume the Commission's Staff will correct in connection with the final Rule.

Rule 506(b)(2)

The purpose of Rule 506(b)(2) appears unclear. In my view, it is unnecessary and should be deleted.

Statutory Basis for Regulation D and Exemptive Rules Thereunder

Release No. 33-5339 does not set forth the statutory basis under the 1933 Act upon which the Commission proposes to rely in adopting Regulation D or the individual Rules thereunder. In my view it is important for the Commission to address this issue directly in the final release adopting Regulation D both as a matter of proper administrative rulemaking and because the statutory basis pursuant to which an individual Rule is promulgated at the federal level will be of critical importance in several states for purposes of determining whether a counterpart exemption at the state level is available. For example, the states of Arizona, Connecticut, and Hawaii, to name just a few, provide an exemption comparable to the federal non-public offering exemption with respect to any transaction that is exempted pursuant to Section 4(2) of the 1933 Act or an exemptive rule adopted thereunder. If Rule 506 is not adopted as a Rule under Section 4(2) of the 1933 Act, or if the Commission neglects to indicate the statutory basis for the Rule, then there may be substantial uncertainties as to the availability of counterpart exemptions at the state level. The purpose of Regulation D should be to promote not disturb coordinated exemptions.

There is clearly no need for the Commission to proceed with hesitance in setting forth the statutory basis for Regulation D or any of the Rules thereunder. In my opinion, the Commission should indicate that the statutory basis for promulgation of Rule 215 and the definition of “accredited investor” used in Regulation D is Section 2(15) and Section 19(a) of the 1933 Act. The statutory basis for Regulation D, including all rules thereunder except Rule 506, should be cited as sections 3(b) and 19(a) of the 1933 Act. Rules 504 and 505 should be specifically identified as exemptive rules under Section 3(b) of the 1933 Act. Rule 506 should be specifically identified as a non-exclusive Rule adopted as a “safe harbor” under Section 4(2) of the 1933 Act and the statutory basis therefor should be cited as Section 19(a) of the 1933 Act. Section 19(a) •by virtue of the Commission’s authority to define, among other things, accounting, technical and trade terms as used in this title, gives the Commission ample authority to adopt Rule 506 as well as the Section 3(b) rules. In this connection, I believe that the term “public offering” or "non-public offering” clearly constitutes a technical or trade term as a result of the usage thereof which has arisen since enactment of the 1933 Act.

Effective Date of Regulation D

Since it is proposed that Regulation D will replace Rules 146, 240 and 242, it is particularly important that the Commission, in adopting Regulation D and establishing an effective date therefor, not take any action which would jeopardize transactions that were commenced prior to the effective date of the rescission of such rules. For example, a particular problem may result from rescission of Rule 146 with respect to what are probably a substantial number of non-public offerings involving Rule 146(g) excluded purchasers of $150,000 or more of securities, who may not constitute “accredited investors” under Rule 501(a). To the extent that such previously commenced Rule 146 offerings may be deemed continuing offerings, the last section of Section 19(a) of the 1933 Act may afford little protection to issuers who commenced such transactions prior to rescission of Rule 146, because there may be acts (collection of installment payments, etc.) which continue after the rescission of Rule 146. Under such circumstances, an issuer is placed in a predicament because it is not possible, even if it were desirable, to conform such offerings Rule 506 retrospectively.

For this reason, it is suggested that the Commission make it clear in the final release adopting Regulation D that rescinded Rules 146, 240 and 242 remain applicable for the completion of transactions which have commenced in reliance upon such rules prior to the effective date of their rescission. Also, because it should be anticipated that there a substantial number of exempt transactions in preparation at any given moment under Rules 240, 242 and 146 the Commission should consider adoption of an effective date of Regulation D which allows sufficient time for issuers and their representatives to complete offerings about to be commenced on the basis of the old rules before rescission thereof. A period of at least 90 days overlap of both sets of exemptions may be appropriate for such purposes

Conclusion

The length of these comments should not be construed as a criticism of the Commission's efforts in proposing Regulation D, As noted in the forepart of this letter, I believe that the Commission and its Staff have made substantial progress in the development of an integrated exemptive scheme at state and federal levels, which, allowing for an initial implementation and familiarization period, should promote certainty and understandability with respect to the exempt transaction process.

Conceptually, I believe that the format of the Regulation and the exemptive Rules thereunder are sound with one notable exception. I believe that it would be a much better approach to include Rule 501(a)(5)-(7) accredited investors instead in the category of excluded purchasers under Regulation D so that informational disclosures and, where appropriate, purchaser representatives may be required, with respect to such persons. A corollary is that the Commission should place less emphasis upon attempting to objectively define those persons who do and do not need to receive informational disclosures and focus instead upon a less burdensome overall informational scheme based upon a test of “substantial equivalence” instead of disclosure identical to 1933 Act registered offering or Regulation A requirements. In this respect, the 60% test for informational disclosures is, in my view, unworkable.

My most substantial criticism of proposed Regulation D is that Section 19(c) of the 1933 Act constitutes a congressional mandate to the Commission and the states to cooperate in reducing burdens on capital formation, particularly small business capital formation. While I agree that the Commission, and hopefully the states through NASAA’s efforts will meet part of this mandate insofar as the regulatory scheme they are considering is a more integrated and understandable scheme, I do not in all honesty believe that the Commission can claim the overall effect of Regulation D, as proposed, will be to reduce capital formation burdens. Specifically, the Commission’s somewhat surprising proposals to require registered broker-dealer involvement if commissions or similar remuneration are paid in connection with an offering, and the revised informational disclosure requirements under Rule 502, in particular the audited financial statement requirement, are, in my view, proposals which will have the overall effect of increasing capital formation burdens and will preclude many issuers, especially small issuers, from being able to rely upon Regulation D exemptions. As a result, the Commission, in my opinion, still has not reached a proper balance between its new mandate to reduce capital formation burdens and its continuing obligation to assure investor protection in connection with exempt offerings.

Very truly yours,
Robert D. Strahota

cc: Mary E.T. Beach, Associate Director
Office of Small Business Policy