

506(c) Offerings: Let's Fix the Verification Rules

Section 201(a) of the JOBS Act repealed the ban on generally soliciting or generally advertising private securities offerings, provided certain conditions were met.

Many people believed that this change in the law would be one of the most dramatic brought about by the JOBS Act. But things didn't go as planned. Today, only a small fraction of private companies raising money generally solicit or generally advertise their offerings. Why is this? Because along the way to passage, the original Section 201(a) was amended to include what many people thought was a reasonable addition, and then the SEC enacted rules requiring something a lot of people don't want to do.

Rule 506(c) Offerings

In Rule 506(c) offerings, a company can generally solicit or generally advertise that they are selling securities but only if:

- All of the investors in the round are accredited, and
- the issuer *verifies* that the investors are accredited.

The [verification rules](#) require companies to ask their investors for their personal tax returns, or their personal financial statements. These verification rules surprised a lot of angels, and essentially made Section 201(a) not quite the improvement in the law we all hoped it would be. Most angel investors don't want to turn over their personal tax returns or personal financial statements as a condition to making an investment in a private company. Similarly, most private companies don't want to put any more hurdles in front of receiving an investment than absolutely necessary.

This is the reason the overwhelming majority of private company securities offerings are still done the old fashioned way, without general solicitation or advertising. This is the the reason almost all companies proceed under Rule 506(b). Rule 506(b) offerings can't be generally solicited or advertised--but they also don't require verification. In a Rule 506(b) offering, you can rely on an investor checking a box averring that they are accredited, as long as your belief that they are accredited is reasonable.

I've quoted Section 201(a) below. The original Section 201(a) did not include the verification language. I have put in bold below the language that was added after [a comment at a House Committee hearing](#) that if companies didn't verify the accredited investor status of their investors, non-accredited investors might be lured into risky investments and lose their money.

I am in favor of repealing this verification requirement, and returning to the original language of Section 201(a). Short of repeal, I think we should change the verification requirements to make

them less intrusive, and more obervant of investors' desire for personal privacy. Perhaps simply allowing investors to certify under penalty of perjury that they are accredited after reading the rules re accreditation and averring that they understand them would be a good compromise.

It would be nice to fix these rules so that Rule 506(c) would be more widely used.

The Language of Section 201(a)

Not later than 90 days after the date of the enactment of this Act, the Securities and Exchange Commission shall revise its rules issued in section 230.506 of title 17, Code of Federal Regulations, to provide that the prohibition against general solicitation or general advertising contained in section 230.502(c) of such title shall not apply to offers and sales of securities made pursuant to section 230.506, provided that all purchasers of the securities are accredited investors. **Such rules shall require the issuer to take reasonable steps to verify that purchasers of the securities are accredited investors, using such methods as determined by the Commission.** Section 230.506 of title 17, Code of Federal Regulations, as revised pursuant to this section, shall continue to be treated as a regulation issued under