



**SUBJECT:** Effect of the National Markets Improvement Act of 1996 (P.L. 104-290) on the Pennsylvania Securities Act of 1972 with Respect to Offers and Sales of Securities in Pennsylvania which are Exempt from Registration under Section 5 of the Securities Act of 1933 pursuant to Rule 506 of SEC Regulation D Promulgated under Section 4(2) of the Securities Act of 1933 Act.

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**TYPE:** Staff Position

**PRIOR RELEASE:** None

President Clinton signed the National Securities Market Improvement Act of 1996 (Federal Act) into law on October 11, 1996. The Federal Act affects the application of the **registration** provisions of state securities laws to transactions that are exempt under rules and regulations issued under Section 4(2) of the Securities Act of 1933 (1933 Act), except that states may impose "notice filing requirements that are substantially similar to those required by rule or regulation under section 4(2) that are in effect on September 1, 1996." (New Section 18(b)(4)(D) of the 1933 Act). This provision of the Federal Act became effective on October 11, 1996.

This Release is intended to provide issuers and issuers' counsel with the position of the staff of the Pennsylvania Securities Commission (PSC) with respect to the treatment of Rule 506 offerings made in Pennsylvania in the context of the Federal Act and the Pennsylvania Securities Act of 1972 (1972 Act). The staff position contained in this Release should be construed as an interim position as PSC staff may modify portions hereof in the future to conform with adoption of uniform filing provisions that may be proposed by the North American Securities Administrators Association (NASAA).

This Release was developed in consultation with the PSC's Attorney Advisory Committee. Consideration also was given to the views expressed by the NASAA Office of General Counsel and lawyers who regularly practice before the PSC in the area of Rule 506 offerings.

## **I. Requirements of the 1972 Act**

**Section 203(d) and the Federal Act.** Most Rule 506 offerings have relied upon the exemption in Section 203(d) and (e) of the 1972 Act, as expanded by Regulation 204.010, to make offers and sales in Pennsylvania. This statutory and regulatory framework of state law continues to apply to Rule 506 offerings subject to the preemptive provisions in the Federal Act. While these provisions (see Section II) are quite substantial, they do permit retention of the notice filing and fee requirements of Section 203(d). **This Release is written in the context that the securities are not registered under the 1972 Act and there is no other exemption available for their sale in Pennsylvania.**

**Non-Payment of Fees Subjects Issuer to Section 201.** It is the staff's position that, until October 11, 1999, state securities registration provisions are not preempted with respect to any issuer who refuses to pay the Section 203(d) filing fee set forth in Section 602(b.1) at the time a notice filing was made or due to be made with the PSC and thereafter fails to promptly remedy a delay in payment or underpayment of that fee (see Section III relating to "Failure to Pay a Fee").

**Suspension Orders.** The Federal Act also permits the states to enforce the notice filing and fee requirements for Rule 506 offerings through the issuance of suspension orders. When an issuer fails to make a notice filing or pay a filing fee, Pennsylvania may issue an order suspending the offer or sale of securities within this state.

**Federal Act Modifications Premised Exclusively on a Rule 506 Offering.** Federal Act modifications to Section 203(d) and (e) of the 1972 Act are premised upon the issuer meeting the requirements of Rule 506 and being able to rely on that regulation for an exemption from the registration provisions of Section 5 of the 1933 Act. If an issuer, however, did not meet the requirements of Rule 506 (even though it might have met the requirements of Rule 504 or 505), failure to comply with the requirements of Section 203(d) of the 1972 Act would result in the sale of securities in violation of Section 201.

It is the position of the PSC staff that the Federal Act affects only offers and sales of securities made in Pennsylvania pursuant to Rule 506 of the 1933 Act and does not apply to the statutory exemption found in Section 4(2) of the 1933 Act. Therefore, an issuer making offers and sales of securities in Pennsylvania in reliance upon the statutory exemption provided in Section 4(2) of the 1933 Act without complying with the requirements of Rule 506 also must comply with Section 203(d) and (e) of the 1972 Act.

## **II. Modifications to Section 203(d) Made by the Federal Act**

It is the position of the PSC staff that the following substantive conditions of Section 203(d) and Regulation 204.010 have been modified by federal preemption through various provisions of the Federal Act:

**Twelve-Month Holding Period.** The requirement that Pennsylvania investors sign an agreement not to sell their investment for a period of 12 consecutive months no longer applies. The requirements under Rule 506, however, remain that purchasers be given notice of federal restrictions on resale, that the securities contain a restrictive legend and that the issuer make reasonable inquiry to determine if the purchaser is acquiring the securities for others.

**Two Business Day Right of Withdrawal.** As Section 207(m) currently is written as applying to certain exempt transactions and Rule 506 transactions no longer will be exempt transactions under the 1972 Act, the two business day right of withdrawal provision no longer is applicable to Rule 506 offerings.

**Prohibition on Sales Compensation to Promoters.** This provision no longer applies but the PSC retains jurisdiction over persons acting as unregistered broker-dealers, agents or investment advisers.

**Prohibition on Advertising and General Solicitation.** While this provision of Section 203(d) no longer applies to Rule 506 offerings as a condition of the exemption, the prohibition on general solicitation in Rule 506 offerings found in Regulation D still pertains.

**Conditions Imposed under Regulation 204.010.** In the context of Rule 506 offerings, the disqualification provisions in Regulation 204.010 conditioning the availability of the expansion of the numerical limitations in the Section 203(d) and (e) exemptions, the requirement to utilize a registered broker-dealer and the investor suitability criteria are no longer effective.

**Use of Prospective Financial Information.** Commission Regulation 609.010 governs the use of prospective financial information in certain offers and sales of securities made in Pennsylvania. Offers and sales to Accredited Investors are exempt from the provisions of this regulation. To the extent that offers and sales of securities in a Rule 506 offering are made to non-Accredited Investors in Pennsylvania in compliance with the requirements of Rule 506, the provisions of this Regulation no longer apply to such offers and sales.

### **III. Notice Filing and Fee Requirements under Section 203(d) for Rule 506 Offerings as Modified by the Federal Act**

**What Form to File.** It is the staff's position that the issuer's obligation to file a notice under Section 203(d), as permitted by the Federal Act, will be satisfied by filing with the PSC a copy of SEC Form D which includes **Part E and the State Appendix manually signed by a person duly authorized by the issuer in the Part E signature block (Notice).** *Staff reminds issuers to respond completely to each item on Form D. Non-responses or unintelligible responses will be treated as a deficiency to the Notice.*

**Documents to be Filed with the Notice.** PSC staff believes that the Federal Act does not preempt the requirement under Section 203(d) for an issuer in a Rule 506

offering to file documents with the PSC which will be given to offerees in Pennsylvania. The PSC has determined, however, to waive the requirement under Section 203(d) to file offering documents for Rule 506 offerings, subject to the ability of staff to request offering documents from time to time in those instances where it is appropriate and necessary for the protection of investors.

**When to File.** It is the staff's position that the issuer's obligation to timely file a Notice, as permitted under the Federal Act, may be satisfied by either:

1. Filing the Notice with the PSC no later than 15 calendar days after the first sale of securities in accordance with Rule 503 of SEC Regulation D (i.e., the first sale made by the issuer); or
2. If the issuer desires to make a sale in Pennsylvania and has not filed a notice within 15 calendar days after the issuer's first sale of securities, filing the Notice no later than the day on which the issuer receives from any person in Pennsylvania an executed subscription agreement or other contract to purchase the securities being offered or the issuer receives consideration from any person in Pennsylvania therefor, whichever is earlier. **N.B. This is the current requirement under Section 203(d) and is suggested for purposes of familiarity and to address the instant situation where the issuer may not have complied with Rule 503 with respect to anticipated PA sales. It is the intention of PSC staff to seek a uniform alternative filing date.**

**Filing Fee to be Paid.** It is the staff's position that the issuer's obligation to pay a Notice filing fee, as permitted under the Federal Act, is satisfied by payment of the Section 203(d) filing fee set forth in Section 602 (b.1) of the 1972 Act based upon the amount of securities to be offered in Pennsylvania as indicated by the issuer on the State Appendix to SEC Form D.

**Failure to Pay a Fee.** It is the staff's position that, until October 11, 1999, an issuer that fails to pay the Section 203(d) filing fee at the time a Notice was filed or due to be filed with the PSC and fails to promptly remedy a delay in the payment of such fee or underpayment of such fee (based on the time the Notice was filed or due to be filed) may be viewed as violating the registration provisions of Section 201 of the 1972 Act. In the case of an underpayment resulting from the issuer underestimating the amount of securities to be sold in Pennsylvania, whether or not the underpayment is promptly remedied will depend upon the circumstances involved.

#### **IV. Sales Made in PA under Rule 506 Prior to October 11, 1996**

It is the staff's position that sales of securities made in Pennsylvania pursuant to a Rule 506 offering for which there was full compliance with the requirements of Section 203(d) remain subject to those requirements and are unaffected by the preemption provisions of the Federal Act.

## **V. Reliance on Section 203(d) as an Alternative to the Federal Act**

If an issuer involved in a Rule 506 offering chooses to rely on the exemption in Section 203(d) of the 1972 Act to avoid the potency of a Section 201 violation in the event that the Rule 506 exemption would not be available, such issuer may do so, provided that there is full compliance with the conditions of Section 203(d). Should the issuer fail to comply fully with the conditions of Section 203(d) but does meet all the requirements of Rule 506, the issuer still could avail itself of the preemption provisions of the Federal Act.

## **VI. Treatment of Certain Filings with the PSC**

**Filing of PSC Form 203-D.** Filing of PSC Form 203-D will be presumed by staff to be a notice filing for the Section 203(d) exemption irrespective of whether the preemption provisions of the Federal Act are available for such offering. These filings will be reviewed for compliance with Section 203(d).

**Filing of SEC Form D and PSC Form D Supplement.** Filing of SEC Form D (even if Rule 506 is checked) and PSC Form D Supplement will be presumed by staff to be a notice filing for the Section 203(d) exemption irrespective of whether the preemption provisions of the Federal Act are available for such offering. These filings will be reviewed for compliance with Section 203(d).

**Filing of SEC Form D with Rule 506 and Rule 505 or 504 Boxes Checked.** Staff will advise the issuer of its position that the preemption provisions of the Federal Act are available only where the issuer meets the requirements of Rule 506 and that failure to comply with Section 203(d) may result in violations of Section 201 in the event that the Rule 506 exemption is unavailable.

## **VII. Failure to Specify on Notice the Amount of Securities Offered in PA**

Issuers are reminded that the Notice to be filed with the PSC requires the issuer to indicate on the state appendix the amount of securities to be offered for sale in Pennsylvania. Under Section 602(b.1), the amount of the Section 203(d) filing fee to be remitted to the PSC with the Notice is based upon the amount of securities to be offered for sale in Pennsylvania. If the amount of securities to be offered in Pennsylvania is not specified in the state appendix of the Notice but the Notice filed by the issuer is accompanied by a filing fee, staff will take the position that the issuer is filing a Notice for the amount of securities represented by the filing fee submitted. Oversales of the amount of securities represented by the filing fee may result in an underpayment of a filing fee and, unless promptly remedied, could subject the issuer to the registration provisions of Section 201 for such sales.

## **VIII. Acknowledgment of Filings by PSC Staff**

**Filing of PSC Form 203-D.** As set forth in Section VI, these filings will be reviewed for compliance with the requirements of Section 203(d). Upon completion

of review, staff will issue the standard acknowledgment letter that nothing has come to the attention of staff that the exemption is unavailable.

**Filing of SEC Form D and PSC Form D Supplement.** As set forth in Section VI, these filings will be reviewed for compliance with the requirements of Section 203(d). Upon completion of review, staff will issue the standard acknowledgment letter that nothing has come to the attention of staff that the exemption is unavailable.

**Filing of a Notice Described in this Release.** Staff will not issue any acknowledgment letter with respect to the filing with the PSC of a Notice described in Section III of this Release.

**Questions concerning this Release should be directed to the Exemptions Section within the Division of Corporation Finance at (717) 787-8059.**

***Alternative formats of this document may be available on request. Call (717) 787-1165 or TDD Users: via AT&T Relay Center 1-800-654-5984.***