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April 3, 2006

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Via e-mail: rule-comments@sec.gov

Securities and Exchange Commission
100 F Street, N.E.
Washington, DC 20549-1090
Attention: Nancy M. Morris,
Federal Advisory Committee Management Officer

Re: File No. 265-23; Release Nos. 33-8666 and 34-53385
Exposure Draft of Final Report of Advisory Committee on Smaller Public Companies

Ladies and Gentlemen:

This letter is submitted on behalf of the Committee on Securities Regulation of the New York City Bar in response to Release Nos. 33-8666 and 34-53385, dated February 28, 2006 (the "Release"), in which the Securities and Exchange Commission (the "Commission") Advisory Committee on Smaller Public Companies (the "Advisory Committee") solicited comments on an exposure draft of its Final Report (the "Draft Report"). The Draft Report contains proposed recommendations of the Advisory Committee on improving the current securities regulatory system for smaller companies. Our Committee is composed of lawyers with diverse perspectives on securities issues, including members of law firms, counsel to corporations, investment banks, investors and academics. Please note that Mr. David Rosenfeld, a member of the Staff of the Commission and a member of our Committee, did not participate in the preparation of this letter or the decision by our Committee to submit this letter to the Commission.

Introduction

Our Committee wishes to comment on one of the suggested changes contained in the Draft Report and takes no position on the balance of the Draft Report.

Recommendation IV.P.5: New Private Offering Exemption for Smaller Companies and Relaxation of Prohibitions Against General Solicitation and Advertising

The Advisory Committee recommends that the Commission, with respect to smaller companies, (i) adopt a new private offering exemption from the registration requirements of the Securities Act of 1933, as amended (the "Securities Act") that does not prohibit general solicitation and advertising for transactions with purchasers who do not need all the protections of the Securities Act's registration requirements and (ii) relax the prohibitions against general solicitation and advertising found in Rule 502(c) under the Securities Act to parallel the "test the waters" model of Rule 254 under the Securities Act. While we support this recommendation, our Committee also proposes that the Commission take this opportunity to expand the application of this recommendation to all companies, not just smaller companies, and broaden the recommendation to allow general solicitation and advertising in private offerings, without significant restriction on content or method, so long as the ultimate purchasers in such offerings are sophisticated investors.¹

Whether or not a transaction qualifies for an exemption from the registration requirements of the Securities Act should depend on the status of the purchasers, rather than on the number or status of offerees or the method by which an issuer located potential offerees and purchasers. An offering in which the ultimate purchasers are "sophisticated investors" (whatever the standard for determining sophisticated investors)² should qualify for an exemption from the registration requirements of the Securities Act, regardless of the means by which such purchasers

¹ The Commission has solicited comment in various rulemakings as to whether the restrictions on general solicitation should be relaxed with respect to certain types of offerings or certain types of investors. See, e.g., The Regulation of Securities Offerings, Release Nos. 33-7606A and 34-40632A (November 13, 1998); Securities Act Concepts and Their Effects on Capital Formation, Release Nos. 33-7314 and 34-37480 (July 25, 1996); Exemption for Certain California Limited Issues, Release No. 33-7285 (May 1, 1996); and Exemption for Certain California Limited Issues, Release No. 33-7185 (June 27, 1995). See also, comments submitted on behalf of the Committee on Federal Regulation of Securities of the American Bar Association's Section of Business Law in connection with the Commission Release on Securities Offering Reform, Release Nos. 33-8501 and 34-50624 (November 3, 2004), in a letter dated February 11, 2005 (noting that elimination of all restrictions on "offers" and "general solicitation" in connection with private offerings is one area for future reform).

² The purpose of this letter is not to comment on the appropriate definition of a sophisticated investor. However, if it would be of assistance, our Committee welcomes the opportunity to discuss an appropriate definition. Regardless of the ultimate measure of a sophisticated investor, so long as the purchasers in a transaction meet the measure, the transaction should qualify for an exemption from the registration requirements of the Securities Act despite the use of general solicitation and advertising in connection with the transaction.

were located.³ The focus should be on protection of actual purchasers. As noted in the Draft Report, "[i]n all the private offerings since the beginning of regulatory time, no offeree has ever lost any money unless he or she became a purchaser." And, as a result, from a policy point of view, no offeree requires the protection of the Securities Act. Purchasers, however, either do or do not need the protection of the Securities Act, based on their financial wherewithal, investment sophistication, relationship to the issuer, institutional status and access to information.

Our Committee believes that, in view of technological advances, including the Internet, it may be both unnecessary and unrealistic to retain any restrictions on "offers" and "general solicitation and advertising" with respect to securities being sold in private offerings. The rationale for continuing to condition private offering exemptions on the absence of general solicitation and advertising is undermined by the public availability of information about private offerings released by third parties. For example, the Internet has made information concerning private offerings, including secondary price quotes, securities ratings, rating agency offering reports and analyst research reports, immediately and widely accessible. Allowing use of today's technologies, such as the Internet, to permit broader access to information in connection with private offerings will not hinder the Commission's ultimate goal of investor protection.

The North American Securities Administrators Association, Inc. has adopted a resolution relating to Internet offers of securities⁴ and a model accredited investor exemption ("MAIE"),⁵ each of which permits general solicitation and advertising. The MAIE's definition of accredited investor is based on the definition of accredited investor contained in Regulation D. As of January 2006, thirty-one states had adopted the MAIE or a similar provision.⁶ It appears that these states have determined that permitting at least some form of general solicitation and advertising is not necessarily contrary to investor protection. Despite widespread state adoption of the MAIE or similar provisions, our Committee notes that the Commission has not adopted a corresponding federal exemption.

As noted in the Draft Report, the Commission has relaxed the general solicitation and advertising restrictions in other contexts.⁷ Regulation A provides a conditional exemption from

³ Just as the exemption contained in Section 4(2) of the Securities Act and the safe harbor contained in Rule 506 of Regulation D should not be conditioned on the absence of general solicitation and advertising, the exemption contained in Rule 144A should not be conditioned on whether offers have been made only to "qualified institutional buyers."

⁴ Resolution Regarding Securities Offered on Internet, NASAA Rep. (CCH) ¶ 7040 (January 7, 1996).

⁵ Model Accredited Investor Exemption, NASAA Rep. (CCH) ¶ 361 (April 27, 1997).

⁶ Qualified Institutional Buyer and Accredited Investor Exemptions, 1 Blue Sky L. Rep. (CCH) ¶ 6471 (January 2006).

⁷ In addition to the relaxation of the general solicitation and advertising prohibition in connection with certain types of private offerings, some limited public announcements relating to private offerings generally are permitted or required. The safe harbors provided by Rule 135c and Rule 135e permit limited public disclosures regarding private offerings, and reporting issuers are required to disclose publicly material private offerings.

registration for small offers and sales of securities (up to \$5,000,000). Rule 254 of Regulation A contains a “test-the-waters” process that allows a company to publish or deliver to prospective purchasers a written document or to make scripted radio or television broadcasts to determine if there is any interest in a securities offering before undertaking a full-blown offering pursuant to Regulation A.

Rule 504 of Regulation D contains an exemption for certain offers and sales of securities not exceeding \$1,000,000. General solicitation and advertising are permissible in connection with Rule 504 offers and sales so long as such offers and sales are made exclusively according to state law exemptions from registration that permit general solicitation and general advertising and sales are made only to accredited investors, as defined under Regulation D.

Regulation CE under the Securities Act provides an exemption from the registration requirements of the Securities Act for certain small offers and sales of securities by California-related issuers to “qualified purchasers”⁸ so long as such offers and sales satisfy the conditions of paragraph (n) of Section 25102 of the California Corporations Code. Paragraph (n) of Section 25102 permits written general announcements of proposed offerings which contain the limited information permitted by the statute.⁹

In addition to the foregoing, in September 2003, the Staff of the Commission issued a report to the Commission on the implications of the growth of hedge funds. Among the recommendations contained in the report was a recommendation that the Commission consider permitting general solicitation and advertising in hedge fund offerings limited to “qualified purchasers” in reliance on Section 3(c)(7) of the Investment Company Act of 1940, as amended. The Staff recognized that allowing hedge funds and other pooled investment vehicles (which limit their investors to sophisticated investors, i.e., “qualified purchasers”) to engage in general solicitation and advertising could help such funds and investment vehicles to identify qualified purchasers, without raising significant investor protection concerns. In the report, the Staff noted that “[t]here seems to be little compelling policy justification for prohibiting general solicitation or general advertising in private placement offerings of Section 3(c)(7) funds that are sold only to qualified purchasers.”¹⁰ Similarly, there is little public policy justification for limiting this recommendation of the Staff to hedge funds and other pooled investment vehicles.

⁸ See Securities Act Concepts and Their Effects on Capital Formation, Release Nos. 33-7314 and 34-37480, at 40 (July 25, 1996) (noting that “qualified purchasers” are similar to “accredited investors” as defined in Regulation D of the Securities Act).

⁹ In the adopting release relating to Regulation CE, the Commission “proposed to provide the same exemption for each state that enacts a transaction exemption incorporating the same standards used by California.” See Exemption for Certain California Limited Issues, Release No. 33-7285, at Part IV.A (May 1, 1996).

¹⁰ In Section VII.F. of the report, the Staff stated:

“We question whether the restrictions on general solicitation for private placement offerings of interests in funds relying on Section 3(c)(7) of the Investment Company Act should be retained.

Instead of relaxing or lifting the ban on the general solicitation and advertising in an ad hoc manner, which could lead to unjustified uneven applications of private offering exemptions, our Committee believes that the recommendation contained in Section IV.P.5 of the Draft Report should be expanded to apply to all companies, not just smaller companies, and should be broadened to allow general solicitation and advertising in private offerings, without significant restriction on content or method, so long as the ultimate purchasers in such offerings are sophisticated investors. The foregoing proposed expansion is intended to reduce the regulatory impediments and cost of accessing the private markets for all companies, consistent with investor protection.

Conclusion

Our Committee applauds the Advisory Committee for undertaking an assessment of the current regulatory system for smaller companies under the securities laws of the United States and for making recommendations for changes.

Please note that this letter does not necessarily reflect the individual views of members of our Committee.

Members of our Committee would be pleased to answer any questions you may have regarding our comments, and to meet with the Staff if that would be of assistance.

Respectfully Submitted,

/s/ Matthew J. Mallow

Matthew J. Mallow,
Committee on Securities Regulation

Drafting Subcommittee

Matthew J. Mallow

Richard B. Aftanas

Unlike a Section 3(c)(1) fund, a Section 3(c)(7) fund can be sold to an unlimited number of investors so long as they are “qualified purchasers.” There seems to be little compelling policy justification for prohibiting general solicitation or general advertising in private placement offerings of Section 3(c)(7) funds that are sold only to qualified purchasers. The staff would be reluctant to ease or eliminate the prohibition on general solicitation for hedge funds or other funds that use the accredited investor standard as their minimum investor criteria. We believe that such an arrangement could increase the level of risk of investment interest by less wealthy investors. On the other hand, permitting funds, including hedge funds, that limit their investors to a higher standard (e.g., “qualified purchasers”) to engage in a general solicitation could facilitate capital formation without raising significant investor protection concerns.”

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