

## **SUPPORTING STATEMENT FOR PROPOSED AMENDMENTS TO RULE 504 OF REGULATION D**

This supporting statement is part of a submission under the Paperwork Reduction Act of 1995 (the “PRA”), 44 U.S.C. §3501, et seq.

### **A. JUSTIFICATION**

#### **1. CIRCUMSTANCES MAKING THE COLLECTION OF INFORMATION NECESSARY**

The Securities Act of 1933 (the “Securities Act”) requires that a registration statement be filed with the Securities and Exchange Commission disclosing prescribed information before securities may be offered for sale to the public. The securities cannot be sold to the public until the registration statement becomes effective. In addition, prospective investors must be furnished a prospectus containing the most significant information in the registration statement. Congress, however, recognized that there are certain situations where there is no practical need for registration or where the public benefits derived from registration are too remote.

Accordingly, a number of exemptions to the registration requirements are contained in the Securities Act. The exemptions that small businesses most typically rely on are those provided by Sections 3(b) and 4(a)(2).

The Commission is authorized under Section 3(b) of the Securities Act to exempt securities from registration if it finds that registration for these securities is not necessary in the public interest or for the protection of investors because of the small amount involved or the limited character of the public offering. Section 4(a)(2) of the Securities Act exempts transactions by an issuer not involving any public offering. Pursuant to this authority, the Commission has adopted various rules (collectively “Regulation D”) establishing several small issues or limited offering exemptions from the registration requirements of Securities Act. The rules (Rules 504, 505, and 506) provide exemptions for offerings that satisfy certain conditions, such as limitations in the type and/or number of investors and, as applicable, limitation in dollar amount.

In Release No. 33-9973,<sup>1</sup> the Commission proposed amendments to Rule 504 of Regulation D to increase the aggregate amount of securities that may be offered and sold in any twelve-month period from \$1 million to \$5 million and disqualify certain bad actors from participation in Rule 504 offerings.

The amendments to Rule 504 of Regulation D contain “collection of information” requirements within the meaning of the PRA. There are two titles for the collection of information requirements contemplated by the amendments. The first title is: “Form D” (OMB Control No. 3235-0076), an existing collection of information.<sup>2</sup> The second title is: “Regulation D Rule

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<sup>1</sup> Exemptions To Facilitate Intrastate and Regional Securities Offerings, Release No. 33-9973 (Nov. 10, , 2015) [80 FR 69786].

<sup>2</sup> Form D was adopted pursuant to Sections 2(a)(15), 3(b), 4(a)(2), 19(a) and 19(c)(3) of the Securities Act (15

504(b)(3) Felons and Other Bad Actors Disclosure Statement,” (OMB Control No. [XXXX-XXXX]), a new collection of information. Although the amendments to Rule 504 do not alter the information requirements set forth in Form D, the amendments are expected to increase the number of new Form D filings made pursuant to Regulation D. Additionally, the mandatory bad actor disclosure provisions that will be required under Rule 504 will contain “collection of information” requirements within the meaning of the PRA.

For all Regulation D offerings, Form D must be filed with the Commission no later than 15 days after the first sale of securities in the offering. The Form D is a simple notice that provides certain information about the issuer and the offering.

As proposed, the amendments to Rule 504 would disqualify issuers from reliance on Rule 504 if such issuer would be subject to disqualification under Rule 506(d) of Regulation D.<sup>3</sup> Consistent with the requirements of Rule 506(e), we proposed to require that the issuer in a Rule 504 offering furnish to each purchaser, a reasonable time prior to sale, a written description of any matters that occurred before effectiveness of any amendments to the rule that may be adopted and within the time periods described in the list of disqualification events set forth in Rule 506(d)(1) of Regulation D,<sup>4</sup> in regard to the issuer or any other “covered person” associated with the offering. For purposes of the mandatory disclosure provision described in the note to proposed Rule 504(b)(3),<sup>5</sup> issuers would be required to ascertain whether any disclosures are required in respect of covered persons involved in their offerings, prepare any required disclosures and furnish them to purchasers.

The Commission would adopt the proposed Regulation D Rule 504(b)(3) Felons and Other Bad Actors Disclosure Statement under the Securities Act. The Regulation D Rule 504(b)(3) Felons and Other Bad Actors Disclosure Statement that would be required to be furnished to investors does not involve submission of a form filed with the Commission and is not required to be presented in any particular format, although it must be in writing. The hours and costs associated with preparing and furnishing the Regulation D Rule 504(b)(3) Felons and Other Bad Actors Disclosure Statement to investors in the offering constitute reporting and cost burdens imposed by the collection of information. An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless it displays a currently valid OMB control number.

## **2. PURPOSE AND USE OF THE INFORMATION COLLECTION**

An important purpose of the Form D notice is to collect empirical data, which provides a continuing basis for action by the Commission either in terms of amending existing rules and regulations or proposing new ones.

The disclosure or paperwork burden imposed on issuers appears in a note to proposed

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U.S.C. 77b(a)(15), 77c(b), 77d(a)(2), 77s(a) and 77s(c)(3)).

<sup>3</sup> See proposed Rule 504(b)(3); see also 17 CFR 230.506(d).

<sup>4</sup> 17 CFR 230.506(d)(1).

<sup>5</sup> See note to proposed Rule 504(b)(3).

Rule 504(b)(3) and pertains to events that occurred before effectiveness of the final rules but which would have triggered disqualification had they occurred after effectiveness. Issuers relying on proposed Rule 504 would be required to furnish disclosure of any relevant past events that would have triggered disqualification under proposed Rule 504(b)(3) that relate to the issuer or any other covered person. If there are any such events, a disclosure statement would be required to be furnished, a reasonable time before sale, to all purchasers in the offering. The disclosure requirement would serve to protect purchasers by ensuring that they receive information regarding any covered persons that were subject to such disqualifying events.

### **3. CONSIDERATION GIVEN TO INFORMATION TECHNOLOGY**

Form D is filed using the Commission's electronic filing system.

The collection of information requirements for the proposed Regulation D Rule 504(b)(3) Felons and Other Bad Actors Disclosure Statement would not be provided to the Commission, either electronically or otherwise.

### **4. DUPLICATION OF INFORMATION**

There is no public source for the information provided on Form D.

We are not aware of any rules that conflict with or substantially duplicate the proposed amendments to Rule 504.

### **5. REDUCING THE BURDEN ON SMALL ENTITIES**

Regulation D is a comprehensive set of exemptions from registration relating to small issues and small issuers. Regulation D was designed to simplify and clarify existing exemptions and to expand their availability to small issuers.

Consistent with the disclosure requirements in Rule 506(e), the proposed Regulation D Rule 504(b)(3) Felons and Other Bad Actors Disclosure Statement would apply to all issuers, including small entities. The requirement would not vary depending on the size of the issuer. We believe that many of the issuers in these Rule 504 private offerings are small entities, but we currently do not collect information on total assets of companies and net assets of funds to determine if they are small entities.

### **6. CONSEQUENCES OF NOT CONDUCTING COLLECTION**

The purpose of collecting Form D information is to provide small businesses with an avenue to offer and sell securities without incurring the costs and burdens traditionally associated with full registration under the Securities Act.

The purpose of the proposed Regulation D Rule 504(b)(3) Felons and Other Bad Actors Disclosure Statement is to alert potential investors about the "bad actor" history of issuers conducting securities offerings as well as the issuer's covered persons. Adopting the proposed

amendments to Rule 504 without the disclosure requirement would weaken the investor protection benefits intended by the disqualification provisions of Rule 506(d) by enabling issuers and other covered persons with a “bad actor” history to avoid disclosing that history to potential investors.

## **7. SPECIAL CIRCUMSTANCES**

No special circumstances at this time.

## **8. CONSULTATIONS WITH PERSONS OUTSIDE THE AGENCY**

The Commission issued a release soliciting comment on the “collection of information” requirement and associated paperwork burdens.<sup>6</sup> Comments on the Commission’s releases are generally received from registrants, investors, and other market participants. In addition, the Commission and staff participate in an ongoing dialogue with representatives of various market participants through public conferences, meetings and informal exchanges. The Commission will consider all comments received. Comments received on the proposal are available at <http://www.sec.gov/comments/s7-22-15/s72215.shtml>. A copy of the proposing release is attached.

## **9. PAYMENT OR GIFT TO RESPONDENTS**

Not applicable.

## **10. CONFIDENTIALITY**

Not applicable.

## **11. SENSITIVE QUESTIONS**

No information of a sensitive nature is required under the collection of information requirements contemplated by the proposed amendments. The information collection for the Regulation D Rule 504(b)(3) Felons and Other Bad Actors Disclosure Statement collects basic Personally Identifiable Information (PII) that may include name, business address, and residential address (for sole proprietor only), telephone/cellular/facsimile number, email address, and Tax ID Number (TIN). The Privacy Impact Assessment (PIA) is provided as a supplemental document.

No information of a sensitive nature is required under the collection of information requirements contemplated by the proposed amendments. The information collection for Form D Notice of sales filed by issuers of securities under Regulation D collects basic Personally Identifiable Information (PII) that may include name, business address, and residential address (for sole proprietor only), telephone/cellular/facsimile number, email address, and Tax ID Number (TIN). The information collection is covered under the System of Records Notices (SORN), which may be found at the following link: <http://www.sec.gov/about/privacy/sorn/secsorn6.pdf>. The Privacy Impact Assessment (PIA) is provided as a supplemental document.

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<sup>6</sup> See Release No. 33-9973.

## 12/13. ESTIMATES OF HOUR AND COST BURDENS

The estimated burden hours and cost burden are made solely for the purposes of the PRA and represent the average burden for all issuers. The cost burden is not derived from a comprehensive or even a representative survey of the costs of Commission rules and forms.

### *Form D (OMB Control No. 3235-0076)*

Form D takes approximately 4 hours per response to prepare and is filed by approximately 25,300 issuers annually. We estimate that 25% of the 4 hours per response (1 hour) is prepared by the issuer for an annual reporting burden of 25,300 hours (1 hour per response x 25,300 responses). We estimate that 75% of the 4 hours per response (3 hours) is prepared by outside professionals retained by the issuer. We estimate the cost of these outside professionals to be \$400 per hour (\$400 per hour x 3 hours per response x 25,300 responses) for a total cost burden of \$30,360,000. Table 1 illustrates the current total annual compliance burden, in hours and in costs, of the collection of information pursuant to Form D.

**Table 1. Estimated paperwork burden under Form D, pre-amendment to Rule 504**

	Number of responses (A)	Burden hours/form (B)	Total burden hours (C)=(A)*(B)	25% Internal issuer time (D)=(C)*.25	75% External professional time (E)=(C)*.75	Professional costs (F)=(E)*\$400
Form D	25,300	4	101,200	25,300	75,900	\$30,360,000

As we are not proposing to alter the information requirements of Form D, our proposed amendments will not affect the paperwork burden of the form, and the burden for responding to the collection of information in Form D will be the same as before the proposed amendments to Form D. However, we estimate that our proposed amendments to increase the aggregate amount of securities that may be offered and sold in any 12-month period in reliance on Rule 504 will increase the number of Form D filings that are made with the Commission.

For purposes of the PRA, we estimate that the proposed amendments to Rule 504 would result in a 20% increase in new Form D filings relying on the Rule 504 exemption,<sup>7</sup> or approximately 200 filings per year, based on the number of new Form D filings reporting reliance on Rules 504 and 505 in 2014.<sup>8</sup> The annual number of new Form D filings rose from 13,764 in

<sup>7</sup> We based this estimate on the impact of a 1997 rule change to Rule 144(d) on the market for Regulation D offerings. In this rule change, the Commission amended Rule 144(d) under the Securities Act to reduce the holding period for restricted securities from two years to one year, thereby increasing the attractiveness of Regulation D offerings to investors and to issuers which resulted in a 20% increase in the number of new Form D filings in each of the three subsequent years. See Release No. 33-9973, at 69826.

<sup>8</sup> In 2014, there were 544 new Form D filings reporting reliance on Rule 504 and 289 new Form D filings reporting reliance on Rule 505. We estimate the number of new Form D filings attributable to the proposed amendments over the next three years as follows: 833 new Form D filings in 2014 relying on either Rules 504 or 505, multiplied by 20% equals 166.6. Rounding 166.6 to the nearest hundredth provides us with an estimate of 200 new Form D filings attributable to the proposed amendments.

2009 to 22,004 in 2014, an average increase of approximately 1,648 Form D filings per year, or approximately 10%. Assuming the number of Form D filings continues to increase by 1,648 filings per year for each of the next three years, the average number of Form D filings in each of the next three years would be approximately 25,300. Accordingly, assuming adoption of these amendments to Rule 504, we estimate there would be approximately 25,500 new Form D filings per year for each of the next three years (i.e., 25,300 plus 200).

Based on this increase, we estimate that the annual compliance burden of the collection of information requirements for issuers making Form D filings after Rule 504 is amended would be an aggregate 25,500 hours of issuer personnel time and \$30,600,000 for the services of outside professionals per year. Table 2 illustrates the estimated total annual compliance burden, in hours and in costs, of the collection of information pursuant to Form D following the amendments to Rule 504.

**Table 2. Estimated paperwork burden under Form D, post-amendment to Rule 504**

	Number of responses (A)	Burden hours/form (B)	Total burden hours (C)=(A)*(B)	25% Internal issuer time (D)=(C)*.25	75% External professional time (E)=(C)*.75	Professional costs (F)=(E)*\$400
Form D	25,500	4	102,000	25,500	76,500	\$30,600,000

*Regulation D Rule 504(b)(3) Felons and Other Bad Actors Disclosure Statement (a Proposed New Collection of Information)*

We anticipate that the Regulation D Rule 504(b)(3) Felons and Other Bad Actors Disclosure Statement would result in an incremental increase in the burdens and costs for issuers that rely on the Rule 504 exemption by requiring these issuers to conduct factual inquiries into the backgrounds of covered persons with regard to events that occurred before effectiveness of the final bad actor disqualification provisions. For purposes of the PRA, we estimate the total annual increase in paperwork burden for all affected Rule 504 issuers to comply with our proposed collection of information requirements would be approximately 830 hours of company personnel time and approximately \$9,600 for the services of outside professionals. These estimates include the incremental time and cost of conducting a factual inquiry to determine whether the Rule 504 issuers have any covered persons with past disqualifying events. The estimates also include the cost of preparing a disclosure statement that issuers would be required to furnish to each purchaser a reasonable time prior to sale.

In deriving our estimates, consistent with those assumptions used in the PRA analysis for the Rule 506 bad actor disqualification provisions,<sup>9</sup> we assume that:

- Approximately 750 Rule 504 issuers<sup>10</sup> relying on Rule 504 of Regulation D would

<sup>9</sup> See Disqualification of Felons and Other ‘Bad Actors’ From Rule 506 Offerings, SEC Rel. No. 33-9414 (July 10, 2013) [78 FR 44730].

<sup>10</sup> Filing data reviewed by the staff of the Commission’s Division of Economic and Risk Analysis indicate that for 2014, 544 issuers claimed Rule 504 and 289 issuers claimed Rule 505 in their Form D filings with the Commission. For purposes of the PRA estimates, and based on the data provided for Rule 504 and Rule 505

spend on average one additional hour to conduct a factual inquiry to determine whether any covered persons had a disqualifying event that occurred before the effective date of the rule amendments; and

- On the basis of the factual inquiry, approximately eight issuers (or approximately 1%) would spend ten hours to prepare a disclosure statement describing matters that would have triggered disqualification under Rule 504(b)(3) of Regulation D had they occurred on or after the effective date of the rule amendments; and
- For purposes of the disclosure statement, approximately eight Rule 504 issuers would retain outside professional firms to spend three hours on disclosure preparation at an average cost of \$400 per hour.

The increase in burdens and costs associated with conducting the proposed factual inquiry for the disclosure statement requirement should pose a minimal incremental effort given that issuers are simultaneously required to conduct a similar factual inquiry for purposes of determining disqualification from the Rule 506 exemption.

#### **14. COSTS TO FEDERAL GOVERNMENT**

We estimate that the cost of preparing the amendments will be approximately \$150,000.

#### **15. REASON FOR CHANGE IN BURDEN**

*Form D (OMB Control No. 3235-0076)*

As explained in further detail in Items 12 and 13 above, the change in burden for Form D corresponds to an estimated 20% increase in the number of Form D filings relying on Rule 504, or approximately 200 filings, under the proposed amendment to Rule 504. The table below illustrates the changes in hour and cost burdens from the burden estimates currently approved by OMB.<sup>11</sup>

	Current Burden		New Burden		Program Change	
	Burden Hours (A)	Cost (B)	Burden Hours (C)	Cost (D)	Burden Hours (E)	Cost (F)
Form D	21,824	\$26,188,800	25,500	\$30,600,000	3,676	\$4,411,200

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offerings in 2014, we assume that approximately 750 issuers would file a Form D indicating reliance on Rule 504 after the effectiveness of the proposed amendments to Rule 504. This figure includes issuers that, before the adoption of these proposed amendments to Rule 504, would have conducted offerings pursuant to Rule 505, but that after the adoption of any such amendments would likely conduct their offerings pursuant to Rule 504.

<sup>11</sup> Columns (A) and (B) represent the most recent burden estimates submitted to OMB. Columns (C) and (D) represent the new burden estimates under the proposed amendments. Columns (E) and (F) represent the program change, which encompasses the change in the burden estimates attributable to the proposed amendments.

*Regulation D Rule 504(b)(3) Felons and Other Bad Actors Disclosure Statement (a Proposed New Collection of Information)*

As explained in further detail in Items 12 and 13 above, the burden relates to new Rule 504(b)(3) disclosure requirements intended to inform Rule 504 offering purchasers of any past disqualifying events associated with the issuer and its covered persons. This is a new collection of information, so there is no change in burden.

**16. INFORMATION COLLECTION PLANNED FOR STATISTICAL PURPOSES**

The information collection is not used for statistical purposes.

**17. APPROVAL TO OMIT OMB EXPIRATION DATE**

We request authorization to omit the expiration date on the electronic version of the Form D Notice of sales filed by issuers of securities under Regulation D. Including the expiration date on the electronic version of the form will result in increased costs, because the need to make changes to the form may not follow the application's scheduled version release dates. The OMB control number will be displayed.

In regard to the Regulation D Rule 504(b)(3) Felons and Other Bad Actors Disclosure Statement, since this requirement does not involve submission of a form filed with the Commission and is not required to be presented in any particular format, although it must be in writing, the Commission is not seeking approval to omit the expiration date.

**18. EXCEPTIONS TO CERTIFICATION FOR PAPERWORK REDUCTION ACT SUBMISSIONS**

Not applicable.

**B. STATISTICAL METHODS**

Not applicable.