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October 5, 2007

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Via Email

Nancy M. Morris, Secretary
U.S. Securities & Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

RE: File Number S7-18-07
Release No. 33-8828

Dear Ms. Morris:

The comments on the above-referenced proposed rulemaking contained herein are solely those of the undersigned and not those of Bybel Rutledge LLP or any of its clients.

New Rule 507

The SEC is proposing to establish, by regulation, a new issuer transactional exemption in which offers and sales of securities would be exempt from registration under Section 5 of the Securities Act of 1933 (the "1933 Act")[1] if sales are made solely to persons meeting the proposed definition of "Large Accredited Investor." New Rule 507 also would permit limited written public announcements of specific information without contravening the prohibition on general advertising and general solicitation applicable to all Regulation D offerings other than offerings meeting the requirements of Rule 504(b)(1)(i)-(iii).

Financial Criteria for Large Accredited Investors. With regard to the proposed tests for determining a Large Accredited Investor, the undersigned concurs with the proposed financial criteria because it provides more guidance to issuers on how to determine appropriate purchasers. Specifically, it eliminates the net worth test currently permitted to determine individual Accredited Investors under Rule 501(a)(5). Not only is it exceedingly difficult for an issuer to conduct any independent verification of a prospective individual Accredited Investor's net worth, but the term is so broad as to include assets on which it is hard to place an informed and independent value (e.g., interests in limited partnerships, collectibles, art, antique cars, vacation homes, RVs, etc.).

[1] 15 U.S.C. §77e.

Limited Advertising Permitted. While the undersigned generally concurs with the Rule 507 proposal, particularly the requirement that the permitted limited public announcement be in writing, it strongly urges the SEC not to adopt the 25 word limitation requirement. Rule 507 is an exemption from registration under the 1933 Act and, unless otherwise indicated, operates as a strict liability provision on issuers. The undersigned is concerned that inadvertent use by an issuer of an announcement exceeding the 25 word limitation, even by one word, could result in loss of the exemption, sale of unregistered securities, and a right of rescission exercisable by purchasers.[2]

Unless the SEC adds "safe harbor" language to Regulation D advising that the Rule 507 exemption would not be lost solely because an issuer engaged in a public announcement which exceeded 25 words which otherwise did not constitute general advertising or general solicitation or include a material misstatement or omission, this requirement could create a trap for the unwary without any corresponding increase in investor protection.

Without elimination of the 25 word limitation or adoption of "safe harbor" language, it is very conceivable that states would assert full jurisdiction over Section 507 offerings where the issuer inadvertently exceeded the 25 word limitation since the issuer would not have complied with all the provisions of Rule 507 and therefore, the purchasers were not "qualified purchasers" under Section 18(b)(3) of the 1933 Act.[3]

No Sales to Persons Who Do Not Qualify as Large Accredited Investors. Although Rule 506 permits sales to 35 non-Accredited Investors who possess such knowledge and experience in financial and business matters that they are capable of evaluating the merits and risks of the offering, many practitioners counsel their clients to accept only Accredited Investors in Rule 506 offerings. Many practitioners view the non-Accredited Investor component of Rule 506 as a "safe harbor" should it become apparent or doubtful that one or more subscribers meets the definition of Accredited Investor. Given the ability to use limited advertising and the requirement that the issuer must communicate the description of a Large Accredited Investor to prospective purchasers, it enhances the usefulness of the exemption to restrict purchasers in such offerings only to Large Accredited Investors.

Authority for Exemption. The undersigned understands that adoption of Rule 507 under Section 28 of the 1933 Act[4] gives the SEC the utmost flexibility in fashioning an appropriate exemption from registration. In contrast, in its proposed rulemaking on pooled investment vehicles, the SEC is constrained by the existing statutory language in

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[2] In commenting on a Model Accredited Investor Exemption proposed by the North American Securities Administrators Association, the Pennsylvania Securities Commission raised similar concerns over a proposal that the brief description of the offering could not exceed ten words (Letter dated February 10, 1997 to Franklin Widman, Deputy Bureau Chief, New Jersey Bureau of Securities, from Robert M. Lam, Chairman, Pennsylvania Securities Commission).

[3] 15 U.S.C. §77r(b)(3).

[4] 15 U.S.C. §77z-3.

Section 3(c)(1) of the Investment Company Act of 1940 (the "1940 Act").[5] Therefore, the SEC should be cognizant that, if Rule 507 is adopted as proposed, persons who do not meet the criteria of Large Accredited Investors could not purchase securities in a Rule 507 offering but could purchase interests in a hedge fund relying on Section 3(c)(1) of the 1940 Act which is making an offering to 100 or fewer Accredited Investors under Rule 506.

Covered Security Status. The SEC proposes to classify purchasers of securities offered and sold in reliance on Rule 507 as "qualified purchasers" under Section 18(b)(3) of the 1933 Act. Although the SEC has made the determination based upon the type of offering in which a person is acting as a purchaser as well as the financial sophistication of the purchaser, the SEC should anticipate that the securities industry will focus almost exclusively on the financial sophistication component (i.e. Large Accredited Investor criteria).

It is extremely important that the SEC be well satisfied with the criteria it finally adopts to determine Large Accredited Investors because it is very likely that, in future, there will be enormous pressure on the SEC to adopt that standard with respect to any offering of securities, not just offerings made in reliance on Rule 507.[6]

The SEC also should be aware of potential issuer confusion over the use of the term "qualified purchaser." Some issuers are very familiar with the definition of "qualified purchaser" in Section 2(a)(51) of the 1940 Act.[7] They are much less familiar with the use of "qualified purchaser" in context of Section 18(b)(3) of the 1933 Act. This quite probably is a matter of education but it may not be the easiest of concepts for issuers or others to grasp. Therefore, should the SEC determine that the financial criteria for determining a Large Accredited Investor is too low, it may wish to consider, for sake of uniformity, adopting the "qualified purchaser" definition in Section 2(a)(51) of the 1940 Act.

Unlike securities which have been designated as covered securities by Section 18(b)(1) of the 1933 Act[8] as to which states are preempted by Section 18(c)(2)(D)[9] from requiring a filing or fee, states may require issuers to make a notice filing, pay a fee, and file consent to service of process with respect to securities designated as covered securities under Section 18(b)(3).[10] Although not having to make any filing with the states would enhance Rule 507 as an effective and cost-efficient method of raising

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[5] 15 U.S.C. §80a-3(c)(1).
[6] Comments to this effect were made during the September 30, 2007 meeting of the Committee on State Regulation of Securities of the American Bar Association in Seattle, WA.
[7] 15 U.S.C. §80a-2(a)(51).
[8] 15 U.S.C. §77r(b)(1).
[9] 15 U.S.C. §77r(c)(2)(D).
[10] Section 18(c)(2)(A) of the 1933 Act; 15 U.S.C. §77r(c)(2)(A).

capital, the SEC cannot ensure that states will not impose notice filing and fee requirements for such offerings.[11]

Proposed Revisions Related to Definition of "Accredited Investor"

For reasons previously cited herein, the undersigned supports adding an alternative investments-owned standard to the Accredited Investor standard. Due to the increased certainty which the definition of investments gives issuers, the undersigned strongly suggests that SEC consider eliminating the net worth test for individuals and allow natural persons to be Accredited Investors either by meeting the income test or an alternative investments-owned test. While it is more likely that non-natural persons may have audited financial statements as to which issuers readily could ascertain the requisite minimum assets, for those which might not, adoption of an alternative investments-owned standard for non-natural persons also would be helpful.

In the proposed definition of investments, it would be useful if the SEC provided guidance on whether or not investments which otherwise met the definition but were held in qualified or non-qualified retirement accounts or deferred compensation plans could be used in meeting the minimum investments-owned criteria.

The undersigned strongly supports an automatic periodic adjustment to the financial criteria for both Accredited Investors and Large Accredited Investors to account for inflationary factors. For exemptions which are premised on a minimum amount of financial sophistication as determined with reference to specific dollar figures, it is important that the level of financial sophistication remain *au currant.*

Proposed Revisions to General Conditions of Regulation D

Proposed Revisions to Regulation D Integration Safe Harbor. The undersigned supports reducing the safe harbor from 180 days to 90 days as proposed. It is the undersigned's experience with clients that most integration issues arise within the 90 to 180 day time frame. We are concerned that a 30 day integration period may invite abuse from certain sectors which may not be involved in legitimate capital raising activities.

Disqualification Provisions. What is most surprising about this proposal is that it appears to be a reversal from long held views of SEC staff that disqualification provisions should not or could not be applied to Rule 504 or Rule 506 offerings. Unlike most SEC releases, this Release contains little policy or legal discussion concerning the proposed imposition of disqualification provisions on such offerings.

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[11] For example, Title 02, Subtitle 02.02.10 of the Code of Maryland Regulations requires the filing of a notice, a consent to service of process, a statement as to the date of the first sale of securities in Maryland, and payment of a fee with respect to the offer or sale of securities which are covered securities under Section 18(b)(3) of the 1933 Act unless the securities or transaction otherwise would qualify for a self-executing exemption under the Maryland Securities Act.

Does the SEC Have Authority to Impose Disqualifications on Rule 506 Offerings?

As a former state securities regulator, we expressed, on several occasions, our concern to the SEC about Rule 506 offerings being made by promoters and control persons who previously had been found to have violated the securities laws.[12] The consistent response from the SEC and SEC staff was that they would undertake referrals of these abuses to the SEC Division of Enforcement[13] since SEC staff had advised the Commission that including a disqualification provision within Rule 506 "may go beyond the statutory underpinnings of Rule 506 and [that] some may view such an approach as a form of merit regulation."[14]

Based upon these SEC expressions, parties interested in various provisions of a proposed Securities Markets Enhancement Act ("SMEA")[15] introduced by then Senator Phil Gramm sought to address concerns about offerings made in reliance on Rule 506 by promoters or control persons who previously had violated the securities laws. The result was an informal consensus among staff members of the North American Securities Administrators Association ("NASAA"), the Senate Banking Committee and the Securities Industry Association ("SIA") to recommend that Congress amend Section 18(b)(4)(D) of the 1933 Act[16] to reinstate state jurisdiction over the Rule 506 offerings where the promoters or control persons had been found to have committed certain violations of the securities laws.[17]

In light of previously expressed SEC positions, such a legislative remedy appeared the only means of addressing investor protection issues raised in certain Rule

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[12] Letter dated March 3, 1998 to Arthur Levitt, Chairman, U.S. Securities & Exchange Commission from Robert M. Lam, A. Richard Gerber and John A Maher, respectively Chairman and Commissioners of the Pennsylvania Securities Commission. Letter dated May 18, 1998 to Brian Lane, Director, Division of Corporation Finance, U.S. Securities & Exchange Commission from John A. Maher, Commissioner, Pennsylvania Securities Commission. Letter dated April 12, 2000 to David Martin, Director, Division of Corporation Finance, U.S. Securities & Exchange Commission from G. Philip Rutledge, Deputy Chief Counsel, Pennsylvania Securities Commission.

[13] Letter dated June 10, 1998 to John A. Maher, Commissioner, Pennsylvania Securities Commission, from William E. Morley, Senior Associate Director, Division of Corporation Finance, U.S. Securities & Exchange Commission.

[14] Letter dated April 16, 1998 to Robert M. Lam, Chairman, Pennsylvania Securities Commission, from Arthur Levitt, Chairman, U.S. Securities & Exchange Commission. Previous SEC staff expressed directly to the undersigned at the time that Rule 506 was merely a "safe harbor" for offerings intending to rely on the Section 4(2) statutory exemption and, since there was no disqualification provision contained in Section 4(2), the safe harbor position set forth in Rule 506 could not contain a disqualification provision.

[15] S.2107, 106th Congress, 2d Session (2000).

[16] 15 U.S.C. §77r(b)(4)(D).

[17] Memorandum dated March 20, 2000 from George Kramer and Jonathan Paret, SIA, to Deborah Fischione, NASAA. Memorandum dated April 12, 2000 from G. Philip Rutledge, Chair, NASAA Federal Legislation Committee to George Kramer and Jonathan Paret, SIA. Memorandum dated May 17, 2000 to George Kramer and Jonathan Paret, SIA, from G. Philip Rutledge, Chair, NASAA Federal Legislation Committee.

506 offerings.[18] Adoption of the proposed rulemaking would eliminate that legislative hurdle. Congress has not amended the 1933 Act to change the language in the Section 4(2) exemption so what has occurred for the SEC to change its position of almost ten years standing. Unfortunately, the Release is devoid of any policy discussion or legal analysis discussing the proposed basis for this change of position. Even more sad are the untold number of investors who have been the victims of investment fraud by persons who, due to previous violations of securities laws, would have met the proposed disqualifications had they existed heretofore.

While the undersigned supports the concept of a disqualification provision in Rule 506 offerings, the SEC should provide, given its prior expressions on the subject, a detailed policy and legal analysis for adopting the proposed disqualification provision.[19]

Furthermore, Preliminary Note 3 to Regulation D states that "an issuer's failure to satisfy all the terms and conditions of Rule 506 shall not raise any presumption that the exemption provided by section 4(2) of the act is not available." It does not appear that the current proposed rulemaking would alter this language. Therefore, could not an issuer with a disqualification rely on Preliminary Note 3 and claim a Section 4(2) exemption? If yes, it is suggested that the SEC revise Preliminary Note 3 to advise issuers with a disqualification as to whether they can or cannot rely on the statutory exemption in Section 4(2).

As Rule 504 was adopted under Section 3(b) of the 1933 Act, the SEC can impose any condition it thinks appropriate and in the public interest and for the protection of investors. Since there are no investor suitability standards generally applicable to Rule 504 offerings,[20] it could be argued that such investors are in more need of protection from offerings made by persons who have been found previously to have violated the securities laws. With respect to Rule 504 offerings, we believe that the SEC has statutory authority to impose a disqualification provision and merely ask why it has taken the SEC so long to recognize the investor protection benefit of such a provision in Rule 504?

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[18] Although S. 2107 (SMEA) was never taken up by the U.S. Senate or enacted by Congress nor did S. 2107 ever contain a provision relating to amending Section 18(b)(4)(D) of the 1933 Act, the Senate Committee on Banking, Housing and Urban Affairs did publish a report on S. 2107dated July 25, 2000. Senate Report 106-360.

[19] For instance, how can a disqualification provision in Rule 506 be distinguished from reasoning employed by the U.S. Supreme Court in *Ernst & Ernst v. Hochfelder*, 425 U.S. 185 (1976) in determining the necessity of proving scienter for violations of Rule 10(b)-5. In ruling that scienter was required to prove a violation of SEC Rule 10b-5, the Court looked to the predicates in the statutory language of Section 10(b) of the 1934 Act pursuant to which the rule was promulgated. It concluded that, since the enabling statutory language used the terms "manipulative" and "deceptive" which require "intent," a violation of any rule adopted thereunder also must contain the element of "intent."

[20] Except for offerings made in reliance on Rule 504(b)(1)(iii).

Third Proposed Disqualification is Overbroad and Should Be Replaced in its Entirety with Language Found in Section 15(b)(4)(H) of the Securities Exchange Act of 1934 Act ("1934 Act").

The undersigned strongly believes that, as proposed, the third proposed disqualification is overly broad and would prohibit issuers from availing themselves of Regulation D because they or a covered person have been found to have committed a technical violation of the relevant securities law, such as failing to file a required report timely.

Some state securities regulators already seek penalties (sometimes by means of a consent order) for issuers who they have determined not to have timely filed their Form D notices with that state for a Rule 506 offering.[21] Under the current proposal, the issuer, because of such a state order, would be barred from using Rule 506 or any other Regulation D exemption in future. This hardly promotes efficient capital formation.

To address the overreaching effect of the third proposed disqualification, we suggest that the SEC adopt the approach it drafted and supported in the amendment to Section 15(b)(4)(H) of the 1934 Act [22]enacted by the Sarbanes Oxley Act of 2002.[23] This created a new statutory disqualification within the meaning of Section 3(a)(39) of the 1934 Act[24] if the *person is subject to a final order of a state securities commission which (i) bars such person from association with any entity regulated by such commission or (ii) constitutes a final order based on violations of any laws or regulations that prohibit fraudulent, manipulative or deceptive conduct.*

Substituting this standard for the third proposed disqualification focuses on egregious conduct of the highest regulatory interest in preventing potential investor abuse while still retaining a disqualification that can arise from violations of state law. Furthermore, this standard was developed by the SEC after taking into account the states' perspective.[25]

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[21] Comment Letter of the Committees on State Regulation of Securities and Federal Regulation of Securities of the American Bar Association on SEC Release No. 33-8814, p. 7.
[22] 15 U.S.C. §78o(b)(4)(H).
[23] Section 604, Sarbanes Oxley Act of 2002, P.L. 107-204, 116 Stat. 745 (July 30, 2002).
[24] 15 U.S.C. §78a(39).
[25] The origin of this provision emanated from investigations and hearings held by the U.S. Senate Permanent Subcommittee on Investigations in 1999 which culminated in the introduction of "The Micro-Cap Fraud Prevention Act of 1999" by Senator Susan Collins on June 9, 1999 as S. 1189, 106th Congress, 1st Session. State views were provided to the Subcommittee (Memorandum dated August 7, 1998 to Larry Gurwin, Chief Investigator to the Minority from G. Philip Rutledge, Deputy Chief Counsel, Pennsylvania Securities Commission and Memorandum dated April 13, 1999 to Elliot Berke, Subcommittee Counsel, from G. Philip Rutledge, Deputy Chief Counsel, Pennsylvania Securities Commission) and to senior SEC staff (Letter dated April 9, 1999 to G. Philip Rutledge, Deputy Chief Counsel, Pennsylvania Securities Commission, from Richard H. Walker, Director, Division of Enforcement, U.S. Securities & Exchange Commission and Letter dated July 2, 1999 to Richard H. Walker, Director, Division of Enforcement, U.S. Securities & Exchange Commission from G. Philip Rutledge, Deputy Chief Counsel, Pennsylvania Securities Commission).

Cease and Desist Orders Should not be the Basis for Disqualification. The fifth proposed disqualification also is problematic. While on its face, the proposal may appear sound, the practice, however, is much different as the laws governing issuance of a Cease and Desist Orders at the state level are different from the provisions of Section 8A of the 1933 Act.[26]

As codified in Section 604(b) of the Uniform Securities Act (2002), states can issue Cease and Desist Orders on an *ex parte* and summary basis. Many state regulators make these orders available to the public upon issuance which sometimes results in the public knowing of the existence of the order before respondents. Under Section 8A of the 1933 Act, the SEC must give notice and opportunity for hearing prior to issuing a Cease and Desist Order. The only exception is when the SEC has made a determination that notice and hearing prior to entry would be impractical or contrary to the public interest. This statutorily imposed predicate is absent from the Uniform Securities Act (2002). Therefore, it is not surprising that the number of Cease and Desist Orders issued by state securities regulators can exceed, by a wide margin, orders initiating substantive administrative proceedings.[27]

In practice, state Cease and Desist Orders, which may accuse the respondent of a potential securities registration violation even when no sale has occurred within the jurisdiction, often are resolved with a consent order which acts to prospectively rescind the original Cease and Desist Order. Under the SEC's proposal, such issuer, while never actually having sold any security to anyone, could be subject to not one, but two of the proposed disqualifications from using Regulation D.

The practice of issuing Cease and Desist Orders varies widely among the states, including differing philosophies ranging from using them sparingly to using them with great frequency. It is not by accident that Cease and Desist were not included in Section 15(b)(4)(H) of the 1934 Act.[28]

SEC to Possess Authority to Waive Disqualifications Based on State Law.

These scenarios lead directly to another area in which the SEC appears to be entering new legal and regulatory territory. Under the Release, the SEC, for good cause shown, could determine that the presence of a disqualification should not be a basis for denial of a Regulation D exemption. While the SEC long has exercised similar authority under current Rule 507(b)(with respect to certain injunctions), it now proposes to exercise similar authority with respect to adjudications and orders issued by state

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[26] 15 U.S.C. §77h-1.

[27] For example, in 2004, the Pennsylvania Securities Commission issued 113 Cease and Desist Orders but only issued 5 Orders to Show Cause. 2005 Annual Report, Pennsylvania Securities Commission, p. 7. South Dakota issued 88 administrative orders in 2004 and 95 in 2006. 2004 Annual Report, South Dakota Department of Revenue and Regulation, p. 44 and 2006 Annual Report, South Dakota Department of Revenue and Regulation, p. 37.

[28] *Supra,* note 25.

securities, banking, and insurance regulators for violations of state laws administered by those agencies. Although it makes administrative sense that the SEC should be able to determine whether a disqualification which it imposes as a condition of the availability of an exemption which it created should be waived, it is conceivable that state regulators and the SEC could differ as to whether a disqualification based upon a violation of state law should be waived.

The SEC should address in its final rulemaking how it will handle requests for waivers of disqualifications based on state laws. Will it contact the state regulator which issued the order or adjudication prior to ruling on the waiver request? If contacted, will the state regulator be given a finite number of days to respond so as not to delay the SEC ruling on the waiver request? If a state regulator objects to the waiver, will the SEC accede to the position of the state regulator? If there is disagreement between the SEC and the state regulator as to granting of the waiver, how will such disagreements be resolved?

Adding a Disqualification for Blank Check Offerings.

The SEC has stated that Rule 507 is modeled upon NASAA's Model Accredited Investor Exemption (the "MAIE"). An important component of the MAIE was a provision which made it unavailable to *an issuer that is in the development stage that either has no specific business plan or purpose or has indicated that its business plan is to engage in a merger or acquisition with an unidentified company or companies, or other entity or person* ("Blank Check Companies"). Such language mirrors the current provision in Rule 504(a)(2).

The SEC itself is familiar with the investor protection and regulatory issues posed by Blank Check Companies and, in response, adopted Rule 419. Regulation D is intended to provide an efficient and effective means for legitimate enterprises to raise capital. The abusive history of Blank Check Companies, as more particularly described in Section 502 of the Penny Stock Reform Act of 1990, provides sufficient evidence and basis for the SEC to deny them the regulatory advantages and lesser regulatory scrutiny afforded by Regulation D.[29]

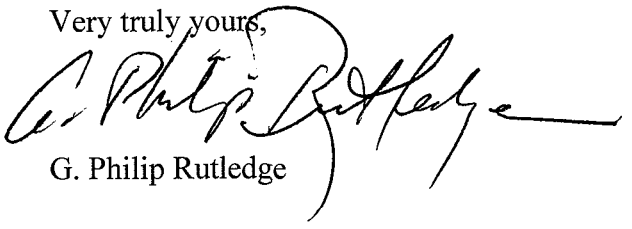
Possible Revisions to Rule 504

The undersigned is aware of certain regulatory issues that have arisen concerning abuse of the MAIE wherein unscrupulous promoters have sought to use it as a conduit to effect a public distribution of securities. The SEC is in a unique position to address this abuse on a national level by revising Rule 504 to make resales of securities offered and

[29] P.L. 101-429 (October 15, 1990). In Section 502(8), Congress found that "the present regulatory environment has permitted the ascendancy of the use of particular market practices, such as 'reverse mergers' with shell corporations and 'blank check' offerings, which are used to facilitate manipulation schemes and harm investors." Section 508 of the act required the SEC to adopt rules imposing certain restrictions on Blank Check offerings which became Rule 419.

sold in reliance on Rule 504(b)(1)(iii) subject to Rule 144. If the SEC were to adopt such a revision, it also would need to revise Rule 144 to permit resales within twelve months from the date of the first sale to other Accredited Investors in order to maintain parity with the MAIE.[30]

Very truly yours,



G. Philip Rutledge

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[30] Paragraph (A) of MAIE as adopted by NASAA, April 27, 1997. *See* www.nasaa.org.