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Global Securities Group Client Alert

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SEC CODIFIES NET WORTH STANDARD FOR ACCREDITED INVESTORS ADOPTED BY DODD-FRANK ACT

On December 21, 2011, the Securities and Exchange Commission (the “SEC”) amended its rules to exclude the value of a person’s primary residence from net worth calculations used to determine whether an individual qualifies as an “accredited investor.” The rule was amended pursuant to the requirements of Section 413(a) of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the “Dodd-Frank Act”) which already implemented the change when it became law on July 21, 2010. The amended rules become effective 60 days after publication in the *Federal Register*.

The Dodd-Frank Act also authorized the SEC to review the definition of “accredited investor” as it applies to natural persons and determine whether other modifications might be necessary. The SEC has concluded that additional modifications are unnecessary at this time. The Dodd-Frank Act requires the SEC to review the “accredited investor” definition in its entirety every four years, commencing in 2014, and empowers it to make additional modifications based on such future review.

The “accredited investor” standards set forth in Rules 215 and 501 under the Securities Act of 1933, as amended (the “Securities Act”), are used to determine the availability of certain exemptions for offerings and sales of securities from Securities Act registration. Specifically, pursuant to Regulation D under the Securities Act, a limited offering of securities pursuant to the Rule 505 or Rule 506 safe harbors does not have to comply with the Rule 502(b) information requirements if sales are made to “accredited investors” and sales to “accredited investors” do not count toward the 35-purchaser limit under the safe harbors.

Under the amended rule, the “accredited investor” \$1,000,000 net worth standard is revised to exclude the value of an individual’s primary residence when calculating net worth. The amendment clarifies that, except as set forth in the next sentence, indebtedness securing the residence, up to the estimated fair market value of the residence at the time the securities are sold, is not included as a liability in measuring net

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worth. In the final rule, the SEC amended this provision to discourage borrowings secured by a primary residence incurred to purchase securities by imposing a 60-day waiting period during which increased borrowings, other than in connection with the purchase of a residence, are to be included in indebtedness for purposes of calculating net worth.

The amended rule also allows individuals who qualified as “accredited investors” prior to the enactment of the Dodd-Frank Act to use the prior net worth standard where (1) the person held a right to purchase the securities prior to July 20, 2010, (2) the person qualified as an “accredited investor” on the basis of net worth when they acquired such right and (3) the person held securities of the issuer (other than the right to purchase) on July 20, 2010.

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