What Every Investor Should Know About Private (Reg D) Offerings

Private offerings are alternative investments also known as Reg D offerings. Reg D is a reference to the exemption from registration that is commonly used for private offerings. Private offerings encompass a variety of alternative investments (e.g., real estate partnerships, oil & gas ventures, promissory notes, leasing deals, etc.). A number of categories of private (Reg D) offerings are included on the list of Top Ten Investor Traps identified by the association of state securities regulators known as NASAA (the National Association of State Securities Administrators). Sometimes private (Reg D) offerings involve ponzi schemes, as did the promissory notes issued by Medical Capital and Provident Royalties. Investors have lost many billions of dollars in private (Reg D) offerings. Moreover, many brokerage firms have gone out of business as a result of selling private offerings.

In addition to the risk of fraud, the problems and risks associated with private (Reg D) offerings include:

- Conflicts – Conflicts of interest involving transactions involving the issuers of private (Reg D) offerings are common. Often times, transactions occur at inflated prices and involve inflated fees.

- Commissions – Selling agents often receive 6% to 7% of the offering proceeds.

- Fees – Like most alternative investments, fees are high (often 15% or more of offering proceeds) and erode returns.

- Illiquidity – Private (Reg D) offerings do not trade on a national securities exchange and are not easily traded. Even in cases where secondary markets are available, they often traded at significant discounts. In addition, early redemption is restricted and the redemption price may be priced below the purchase price or current price.

- Opacity – Lack of transparency with regard to the management and operation of the issuers of private (Reg D) offerings, as well as misrepresentations and lack of disclosure of particular risks affecting the investment, are problems noted by regulators.

- Due Diligence – Brokerage firms that sell private (Reg D) offerings often fail to perform adequate due diligence, often relying on assertions by the promoters rather than conducting an independent investigation.

- Volatility – The supposed lack of volatility is an illusion caused by lack of trading and misleadingly failing to adjust the purchase price to reflect changes in the real estate market and the particular assets held by the private (Reg D) offering.

- Valuation – The lack of trading means there is no market value. Private (Reg D) offerings must be valued using models and guesswork. They are often misleadingly valued at cost on statements sent to investors.

- Distributions – Distributions are subject to suspension and may be eliminated. They often represent a return of investor capital and consist of borrowed funds instead of profits from operations.

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