



## **EQUITY CROWDFUNDING IS AWESOME!**



Equity Crowdfunding is Awesome! There, I have said it. Most lawyers seem to be against equity crowdfunding under new [Regulation Crowdfunding](#) and Title III of the JOBS Act, especially those at big firms. They talk about how investors will get ripped off by shysters and startup companies that have no chance of success. They also complain about the limit of \$1 million for any equity crowdfunding raises undertaken within a period of 12 months. I have a totally contrary opinion. I believe that equity crowdfunding will become the new way that legitimate early stage companies raise capital to grow their businesses. Equity crowdfunding will be the new way that startups raise capital from friends and family. Since most entrepreneurs don't have a huge network of high net worth friends, equity crowdfunding will allow them to ask for small amounts (\$100 or \$300) from a large number of their actual friends, acquaintances, fans and social media contacts. I also believe that the investors will be protected because they will receive full disclosure by way of a Form C offering statement and the amount of their investment is limited. Besides, SEC enforcement is always standing by to pounce on the fraudsters. Equity crowdfunding is an excellent tool for entrepreneurs. It allows an entrepreneur to raise capital from both accredited and non-accredited investors.

To capitalize on the tools provided by Regulation Crowdfunding, entrepreneurs should work with their counsel to prepare a Form C offering statement and file it with the SEC.

Securities may only be sold through one intermediary or funding portal. The funding portal must be a funding portal member of FINRA ([here is the list of funding portal members so far](#)) or a registered broker dealer. The Form C offering statement resembles a private placement memorandum. Once the Form C offering statement is close to ready, the entrepreneur will then set up a landing page on the portal using the information from the Form C offering statement and providing other information. Of course, entrepreneurs will want to have a compelling video, pictures and other marketing collateral that they can upload to the portal to make their offering more attractive. Once everything is up on the portal and the Form C is filed with the SEC, entrepreneurs can begin marketing their offering immediately. The SEC does not typically review the Form C, so there is no delay resulting from an SEC comment and review period. There are certain restrictions on what can be said in the advertising material. For example, an advertisement must either be in the form of a tombstone that has limited information about the terms of the offering or be a general advertisement that does not mention the terms of the offering. Tombstones and general advertisements must refer potential investors to the funding portal.

The SEC published an excellent summary of [Regulation Crowdfunding](#) called “[A Small Entity Compliance Guide for Issuers](#).” I urge you to review it if you are interested in getting into the the details of Regulation Crowdfunding. Following is a brief summary of Regulation Crowdfunding’s requirements taken largely from the SEC’s guide.

- **Maximum Amount of Raise.** The maximum amount that an issuer can raise is \$1 million in a 12-month period. The \$1 million limit includes securities it has already sold (including amounts sold by affiliates, which is important for private equity funds to keep in mind when using equity crowdfunding to raise capital for their portfolio companies) in reliance on Regulation Crowdfunding during the 12-month period preceding the expected date of sale, plus the amount the issuer intends to raise in reliance on Regulation Crowdfunding in the current offering.
- **Investor Limits.** Individual investors cannot invest more than the following amounts over the course of a 12-month period in equity crowdfunding transactions:
  - If either of an investor’s annual income or net worth is less than \$100,000, then the investor’s investment limit is the greater of: \$2,000 or 5 percent of the lesser of the investor’s annual income or net worth.
  - If both annual income and net worth are equal to or more than \$100,000, then the investor’s limit is 10 percent of the lesser of their annual income or net worth.
  - During the 12-month period, the aggregate amount of securities sold to an investor through all Regulation Crowdfunding offerings may not exceed \$100,000, regardless of the investor’s annual income or net worth.

- ***Transactions Conducted Through a Portal.*** Each Regulation Crowdfunding offering must be exclusively conducted through one online platform. The portal operating the platform must be a broker-dealer or a funding portal that is registered with the SEC and FINRA.
- ***Eligibility*** The companies that cannot use Regulation Crowdfunding include:
  - non-U.S. companies;
  - companies that already are Exchange Act reporting companies;
  - certain investment companies;
  - companies that are disqualified under Regulation Crowdfunding's disqualification rules;
  - companies that have failed to comply with the annual reporting requirements under Regulation Crowdfunding during the two years immediately preceding the filing of the offering statement; and
  - blank check companies, i.e., companies that have no specific business plan or have indicated their business plan is to engage in a merger or acquisition with an unidentified company or companies.
- ***Disclosure by Issuers.***
  - Any issuer conducting a Regulation Crowdfunding offering must file its offering statement on Form C with the SEC through the EDGAR system and with the portal facilitating the crowdfunding offering.
  - Form C requires disclosure regarding the following:
    - information about officers, directors, and owners of 20 percent or more of the issuer;
    - a description of the issuer's business and the use of proceeds from the offering;
    - the price to the public of the securities or the method for determining the price,
    - the target offering amount and the deadline to reach the target offering amount,

- whether the issuer will accept investments in excess of the target offering amount;
  - certain related-party transactions; and
  - a discussion of the issuer's financial condition and financial statements.
- Form C also has financial statement requirements. The financial statement requirements are based on the amount offered and sold in reliance on Regulation Crowdfunding within the preceding 12-month period:
    - Raising \$100,000 or less: Financial statements of the issuer and certain information from the issuer's federal income tax returns, both certified by the principal executive officer.
    - Raising more than \$100,000 but not more than \$500,000: Financial statements reviewed by a public accountant that is independent of the issuer.
    - Raising more than \$500,000:
      - First time equity crowdfunding raise: Financial statements reviewed by a public accountant that is independent of the issuer.
      - Not a the first equity crowdfunding raise: Financial statements audited by a public accountant that is independent of the issuer.
  - Amendments to Offering Statement. An issuer can amend its Form C to disclose changes, additions or updates to information. An amendment is required for changes, additions or updates that are material, and in those required instances the issuer must reconfirm outstanding investment commitments within 5 business days, or the investor's commitment will be considered cancelled.
  - Progress Updates. An issuer must provide an update on its progress toward meeting the target offering amount within 5 business days after reaching 50% and 100% of its target offering amount. These updates will be filed on Form C-U. If the issuer will accept proceeds over the target offering amount, it also must file a final Form C-U reflecting the total amount of securities sold in the offering. If, however, the portal provides frequent updates on its platform regarding the progress of the issuer in meeting the

target offering amount, then the issuer will need to file only a final Form C-U to disclose the total amount of securities sold in the offering.

- Annual Reports. An issuer that sold securities in a Regulation Crowdfunding offering is required to provide an annual report on Form C-AR no later than 120 days after the end of its fiscal year. The report must be filed on EDGAR and posted on the issuer's website. The annual report requires information similar to what is required in the offering statement, although neither an audit nor a review of the financial statements is required.
- ***Limits on Advertising***. An issuer may not advertise the terms of a Regulation Crowdfunding offering except through either a tombstone type advertisement or a general advertisement that does not mention the offering terms.
  - A tombstone type advertisement can include no more than the following:
    - a statement that the issuer is conducting an offering pursuant to Section 4(a)(6) of the Securities Act, the name of the portal through which the offering is being conducted, and a link directing the potential investor to the portal's platform;
    - the terms of the offering, which means the amount of securities offered, the nature of the securities, the price of the securities, and the closing date of the offering period; and
    - factual information about the legal identity and business location of the issuer, limited to the name of the issuer of the security, the address, phone number, and website of the issuer, the e-mail address of a representative of the issuer, and a brief description of the business of the issuer.
  - An issuer may also publish a general advertisement that does not discuss the terms of the offering. "Terms of the Offering" is described in the second bullet point under tombstone advertisement above. So, as long as you do not mention the terms of the offering and so long as you refer potential investors to the portal that your offering is listed on, you can publish all kinds of information about your company, state that you are undertaking an equity crowdfunding offering and refer investors to the portal. Make sure, however, that there is a basis in fact and that your advertisements are not exaggerated or misleading.
- ***Paying Promoters***. An issuer is allowed to compensate others to promote its crowdfunding offerings through communication channels provided by an portal,

but only if the issuer takes reasonable steps to ensure that the promoter clearly discloses the compensation with each communication.

- ***Restrictions on Resale.*** Securities purchased in a crowdfunding transaction generally cannot be resold for a period of one year, unless the securities are transferred: (1) to the issuer of the securities; (2) to an “accredited investor;” (3) as part of an offering registered with the Commission; or (4) to a member of the family of the purchaser or the equivalent, to a trust controlled by the purchaser, to a trust created for the benefit of a member of the family of the purchaser or the equivalent, or in connection with the death or divorce of the purchaser or other similar circumstance.

If you are interested in learning more about equity crowdfunding or need help deciding whether it is appropriate for your company, please contact me. I would be happy to discuss this with you. I can be reached at [info@bevilacquaplbc.com](mailto:info@bevilacquaplbc.com) or by phone at 202-203-8665.