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# SEC ADOPTS EQUITY CROWDFUNDING RULES

On October 30, 2015, the Securities and Exchange Commission adopted the final rules for equity crowdfunding under Title III of the JOBS Act. The crowdfunding rules will not go into effect for 180 days, an unusually long lead time, to allow newly-created funding portals adequate time to register with FINRA or another similar self-regulatory organization. The SEC also amended Rules 147 and 504 to coordinate with intrastate equity crowdfunding exemptions now permitted in more than half the states.

Key components of the new rules include the following:

Crowdfunding will be limited to raises of not more than $1 million in a 12-month period. All such offerings must be conducted through intermediaries, either registered broker/dealers or newly-created funding portals, which themselves must be registered with both the SEC and an SRO, such as FINRA.

The issuer must provide basic information about itself and the offering on new Form C, as well as financial information for the most recent two years or such shorter period of time that the issuer has been in business. In a change from the proposed rules, the offering information can be provided in a question-and-answer format or be freely written.

For offerings under $100,000, only issuer-certified financial statements need be provided. For offerings between $100,000 and $500,000, the financial statements required auditor review. Offerings between $500,000 and the $1,000,000 limit require full audit; however, in a crucial change from the proposed rules, a first-time issuer can use reviewed financial statements, unless they already have audited financial statements, thereby reducing the transaction costs of such an offering.

In another significant change from the proposed rules, the SEC tightened individual investor limits. Investors will be limited to the *lesser* of $2,000 or 5% of annual income or net worth, if both annual income and net worth are less than $100,000; or the *lesser* of 10% of annual income or net worth, if either annual income or net worth is greater than $100,000, with a maximum $100,000 total investment in all crowdfunding offerings in a 12-month period, regardless of net worth or net income. It may be very difficult, if not impossible, to enforce these limits on private investors.

An issuer will have an annual reporting obligation to the SEC post-offering. However, the financial information to be provided need not be audited or reviewed, unless such financial statements already exist. The annual reporting obligation will continue until the issuer becomes a full reporting company, has *de minimis* shareholders and/or assets, fully redeems the offering or dissolves.

As noted, all crowdfunding offerings must be conducted through an intermediary, either a broker/dealer or newly-registered funding portal. FINRA has already proposed registration rules to register new funding portals, which rules await SEC action.

As regulated gatekeepers, funding portals will be required to provide information about posted offerings as well as general information about Title III crowdfunding. Funding portals will also be required to conduct background checks on the issuer and its affiliates.

Offerings must be posted for at least 21 days before sales can be made, allowing time for investors to review and reflect on the offering.

While funding portals may not receive commissions for their efforts in assisting the offering, in a change from the proposed rules, the portals may have a financial interest in the issuer if it is on the same terms as the offering.

In companion action, the SEC also created a new exemption from Federal registration under Rule 147 and amended the offering limit of Rule 504 of Regulation D, in recognition of the intrastate crowdfunding exemptions that now exist in more than half the states.

Under the new Rule 147 exemption, any offers made anywhere are exempt, provided that sales are only made to investors who are resident of the state in which the issuer maintains its principal place of business. Additionally, to rely on the new Federal exemption, there must be either state registration or an exemption from state registration for the intrastate offering, and the state exemption must include an aggregate raise limit of $5 million as well as investor limits. Finally, at least 80% of the assets, revenues or use of proceeds must be in-state. There will be a nine-month holding period before such securities can be resold out-of-state.

Rule 504 has been amended to increase the aggregate amount that can be raised in such an offering from $1 million to $5 million. Additionally, the Dodd-Frank “bad actor” exclusion has been extended to Rule 504, so that this protection now applies uniformly across Regulation D.

It will be at least a few weeks before the rules are published in the Federal Register and it would not be unprecedented to see other elements of the rules introduced or changed in the formal text that were not discussed at the SEC meeting.

If you have questions regarding the new rules, the other capital raising innovations under the JOBS Act (general solicitation of private offerings and Reg A+ mini-IPOs), or specific transactions, please contact:

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