

Equity Crowdfunding

Regulation A+ Creates 'Mini-IPOs' For Average Investors

It also sows confusion: Is Reg A+ a healthy way for startups to raise capital?

By David M. Freedman and Matthew R. Nutting

The Jumpstart Our Business Startups (JOBS) Act of 2012 introduced several new ways for private companies to raise capital. Title II of the JOBS Act made general solicitation legal in certain Regulation D offerings for accredited investors. Title III established equity crowdfunding and opened the door for non-accredited (average) investors.

In March 2015, the focus shifted to Title IV. The SEC issued final rules under Title IV, colloquially known as Regulation A+, on March 25. The rules will go into effect in June 2015, and then companies can add Reg A+ to the growing list of financing options for private companies.

Under Title IV, the moribund Regulation A exemption was expanded from a \$5 million raise limit to a \$50 million limit, and it now preempts blue sky review (i.e., no need for approval by every state in which the offering is made) for offerings over \$20 million. Blue sky review is still required for offerings under \$20 million.

Some Regulation A+ offerings are listed through online offering platforms. Such platforms may be dedicated to Reg A+ offerings, or they may feature (as does Wefunder, for example) a mix of Regulation D and Regulation A+ offerings. But Reg A+ offerings are not *required* to go through intermediaries. Moreover, these new offerings are allowed to “test the waters,” measuring potential interest by investors, before undertaking the obligations of an offering.

Even when a Reg A+ offering gets listed on an online platform like EarlyShares, the issuer has no obligation to conduct any sort of Q&A forum or chat with potential investors, as is customary on Reg D and intrastate offering platforms (and will be required on Title III equity crowdfunding portals). So can we say that Reg A+ is crowdfunding? We don't think so, but many people apply the term “crowdfunding” loosely to a broad array of funding platforms, even some that exclude the *crowd* of non-accredited investors.

Before the JOBS Act, Regulation A issuers could sell unrestricted securities to non-accredited as well as accredited investors. The expanded Reg A+ still lets non-accredited investors participate, but it limits their annual investment in offerings above the \$20 million threshold to 10 percent of their income or net worth, whichever is greater. All investors can invest an unlimited amount in offerings up to \$20 million.

By contrast, the offering platforms that list Reg D offerings, under Rules 506(b) and 506(c), are open only to accredited investors. Platforms that feature intrastate offerings (under Section 3(a)(11) of the Securities Act of 1933) are open to accredited and non-accredited investors alike, but only in a dozen or so states and the District of Columbia—although the number of states is growing.

There has been much confusion in the media about Reg A+, as some reporters have referred to it as “an opportunity for non-accredited investors to buy equity in startups,” whereas Title IV was originally structured mainly for growth- and later-stage companies that are not quite ready to file IPOs. New York securities lawyer Brian Korn calls Reg A+ the “minor leagues for IPOs,” and others refer to it as the “mini-IPO,” as issuers are required to go through a “scaled-down registration”¹ process and file a prospectus-like document called an “offering circular” with the SEC. The benefits of Reg A+ for seed-stage and startup companies seem limited mainly because offerings up to \$20 million still require blue sky review and compliance, which can be very costly and time-consuming. Time will tell whether seed-stage and startup companies try to take advantage of Reg A+ rather than (or in addition to) Reg D, intrastate, or someday Title III equity crowdfunding.

Kinds of Equity Offerings on Internet-based Platforms					
	Online Launch	Raise Limit in 1 Year	Investor Status	Investment Limit	Intermediary Required?
Reg A+ Tier 1	2015	\$20 million	All investors	No limit	No
Reg A+ Tier 2	2015	\$50 million	All investors	Depends on income & net worth	
Reg D Rule 506(b)	2011	No limit	Accredited only	No limit	No
Reg D Rule 506(c) ²	2013				
Intrastate Equity Crowdfunding	2013 (Georgia was first)	Ranges \$1m to \$5m	All investors	Depends on income & net worth	Varies with state
Title III Equity Crowdfunding	Maybe 2016	\$1 million ³	All investors	Depends on income & net worth	Yes: online portals ⁴

The Confusing Universe of Offering Platforms

As a result of the various kinds of private securities offerings that can be listed online, and the conflicting definitions of “equity crowdfunding,” there is much confusion in the marketplace—even among professionals who practice in the area of private securities, but especially among

¹ Andres J. Trujillo, “Making History at the SEC: Reg A+ is Better than Expected,” CrowdfundBeat, undated (probably March 26, 2015).

² Rule 506(c) allows general solicitation under Title II of the JOBS Act. (Both tiers of Reg A+ allow general solicitation.)

³ Congress may increase this limit to as much as \$5 million, maybe as soon as summer 2015.

⁴ Title III offerings may appear on non-broker-dealer funding portals that are registered with the SEC or on broker-dealer platforms.

entrepreneurs and investors—about the differences between the exemptions and platforms where you find these offerings.

The table above shows the most important differences, from an investor’s point of view, between the four kinds of equity offerings that you will (eventually) find on online offering platforms, assuming Title III equity crowdfunding will someday emerge from regulatory hell. We expect that Congress will fix Title III of the JOBS Act, probably in 2015, the SEC will issue final rules under Title III, and equity crowdfunding portals will launch in 2016.

We use the term “equity crowdfunding” only in relation to (a) Title III of the JOBS Act, which requires issuers to interact with all (including non-accredited) investors on funding portals; and (b) those states where intrastate securities exemptions allow equity offerings to be listed on online funding platforms and which allow non-accredited investors to invest and interact with issuers. In fact, Title III (and the SEC’s proposed rules thereunder) is the only part of the JOBS Act that specifically mentions the crowd, crowdfunding, or funding portals. Some intrastate exemptions, but not most, refer to equity crowdfunding or funding portals as intermediaries.

Much of what you hear about equity offering platforms and crowdfunding is speculation. We will soon see how the various JOBS Act financing schemes really work, what kinds of companies use which exemptions, and how investors perceive value in each new opportunity. Looking ahead, it is possible that Reg. A+ will work alongside rather than overlap with Title III equity crowdfunding and Reg D offerings, to provide a seamless progression of capital-raising options for companies, from early seed-stage startups using Title III, on to early growth-stage companies fueling expansion with Reg D, and then to Reg. A+ for pre-IPO later growth.

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David M. Freedman, based in Chicago, has worked as a financial and legal journalist since 1978 (www.freedman-chicago.com). Matthew R. Nutting practices corporate law with the firm Coleman & Horowitz in Fresno, CA (www.ch-law.com). Freedman and Nutting are coauthors of *Equity Crowdfunding for Investors*, to be published by Wiley & Sons in June 2015.