

SEC Adopts Final Crowdfunding Rules, Completing JOBS Act Rulemaking

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On October 30, the **Securities and Exchange Commission** adopted “**Regulation Crowdfunding**,” which consists of final rules that will enable eligible companies to raise up to \$1 million in capital in any 12-month period by offering securities through SEC registered intermediaries in crowdfunding transactions on the Internet. The long-awaited crowdfunding rules implement the exemption from registration under the Securities Act of 1933 (Securities Act) provided by Section 4(a)(6) of the Securities Act, which was adopted pursuant to the Jumpstart Our Business Startups (JOBS) Act. The exemption will be available to US issuers, other than reporting companies under the Securities Exchange Act of 1934 (Exchange Act), certain investment companies, blank check companies or companies that have indicated that their business plan is to engage in a merger or acquisition with an unidentified company, companies that have failed to comply with annual reporting requirements under Regulation Crowdfunding within two years prior to a proposed offering, and issuers that are disqualified under “bad actor” provisions.

The crowdfunding rules outline limitations on the aggregate amount any person may invest in in all crowdfunding offerings in any 12-month period. An individual investor with an annual income or net worth of less than \$100,000 will only be permitted to invest up to the greater of (1) \$2,000 and (2) 5 percent of the lesser of his or her annual income or net worth. If an individual investor has an annual income *and* net worth greater than or equal to \$100,000, he or she may invest up to 10 percent of the lesser of his or her annual income or net worth. Regardless of an investor’s annual income or net worth, an individual investor will not be permitted to purchase more than \$100,000 worth of securities in offerings under Regulation Crowdfunding in any 12-month period.

The crowdfunding rules outline disclosure requirements that issuers must satisfy in connection with an offering and in annual reports, which an issuer will be required to file after completing an offering in reliance on the crowdfunding exemption. In connection with a crowdfunding offering, an issuer will be required to file a “Form C” with the SEC and provide to potential investors and the applicable intermediary disclosure regarding the issuer and the offering, including the price for the security (or the method for determining the price), the target offering amount (as well as the deadline for reaching the target, and whether the issuer will accept investments in excess of the target), information relating to: (1) the use of proceeds from the offering; (2) the officers, directors and owners of 20 percent or more of the company; (3) related party transactions; (4) the company’s business and financial

condition; and (5) the company's financial statements, which must be audited in certain circumstances (as discussed below).

The financial statements provided to the SEC, investors and the applicable intermediary in connection with an offering under the crowdfunding rules must: (1) be prepared in accordance with US generally accepted accounting principles; (2) cover the two most recently completed fiscal years of the issuer (or shorter period since the inception of the issuer, if applicable); and (3) be certified (and accompanied by tax returns), reviewed or audited, depending upon the aggregate amount of securities offered by the issuer during the preceding 12-month period. Specifically:

- In the case of an issuer offering \$100,000 of securities or less in reliance upon the crowdfunding rules during the applicable 12-month period, financial statements must be certified by the principal executive officer of the issuer to be true and complete in all material respects, and must be accompanied by disclosure of the amount of total income, taxable income and total tax, as reflected in the issuer's federal income tax return (in lieu of filing a copy of the tax return), and such disclosure must be certified by the principal executive officer of the issuer to accurately reflect the information in such return.
- In the case of an issuer offering more than \$100,000, but not more than \$500,000, of securities in reliance upon the crowdfunding rules during the applicable 12-month period, financial statements must be reviewed (but not audited) by an independent public accountant.
- In the case of an issuer offering more than \$500,000 of securities in reliance upon the crowdfunding rules during the applicable 12-month period, financial statements must be audited by an independent public accountant, except that (in contrast to the SEC's proposed crowdfunding rules) under the final rules, a company offering more than \$500,000 of securities pursuant to the crowdfunding exemption for the first time would be permitted to provide reviewed rather than audited financial statements.

In each of the above cases, however, audited financial statements must be provided if financial statements that have been audited by an independent public accountant are available.

Companies relying on the crowdfunding exemption will be required to offer their securities through a registered SEC intermediary, which may be an online "funding portal" or a broker dealer. Issuers will only be entitled to register with one intermediary in any 12-month period. The funding portals will be required to register with the SEC, utilizing Form Funding Portal and become members of the Financial Industry Regulatory Authority, which has also proposed a set of seven rules and related forms that will govern the registration of crowdfunding portals with FINRA. Intermediaries will be subject to various regulatory requirements, many of which impose a "gatekeeping" function on the portals. Specifically, crowdfunding portals will be required to furnish educational materials to prospective investors, provide communication channels for the "crowd" to discuss offerings, take measures to reduce fraud (including measures to form a reasonable basis for believing that an issuer complies with Regulation Crowdfunding), make information that a company is required to disclose available to the public on the portal's platform throughout the offering period and for a period of at least 21 days before any security may be sold in the offering, and establish a reasonable basis for believing each investor complies with applicable investment limitations.

Holders of securities sold in a crowdfunding offerings will generally be required to hold all securities purchased for a least one year before engaging in sales. Holders of securities sold under the

crowdfunding rules will not be counted for purposes of determining whether an issuer is required to register under Section 12(g) of the Exchange Act, so long as the issuer is current in its annual reporting, has less than \$25 million in total assets as of the end of its most recently completed fiscal year and engages a transfer agent.

The newly adopted rules are effective 180 days after publication in the *Federal Register*. Funding portals may begin the registration process with the SEC on January 29, 2016.

Click [here](#) to view a complete text of the SEC's adopting release with respect to the final rules.

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