The Jumpstart Our Business Startups Act of 2012 (the “JOBS Act”), was promoted as a new piece of legislation creating groundbreaking additional pathways to funding for companies, which was especially highlighted by the 2008 financial crisis. Two provisions in the JOBS Act, created “Regulation” crowdfunding and “Reg A+” offerings, were particularly focused on early stage and emerging growth companies’ financing needs.

The goal of Regulation crowdfunding was to give parents, relatives and friends of founders of start-up companies who were not accredited investors, a path to fund these ventures. Reg A+, on the other hand, was more of an overhaul of then-existing Regulation A, designed to boost its use by increasing the offerings limits and having a certain type (Tier 2 Reg A+ offerings) pre-empt state securities laws like Rule 506 under Regulation D.

1. The Limited Interest in Early Stage Crowdfunding and Reg A+ Offerings

Early signs indicated that Regulation crowdfunding was a bust. From May 2016 through December 31, 2018, the SEC estimated that there were approximately 1,351 Regulation crowdfunding offerings, raising a modest total of $108 million.

A recurring explanation for the little interest in this type of financing was that Regulation crowdfunding offerings were capped at $1.07 million through a 12-month
period, thus limiting its attractiveness due to the high costs and complexity of raising money and compared to a classic Rule 506 offering. Specifically, crowdfunding issuers must make certain disclosures, which can be costly and burdensome—and seemingly at odds with the very purpose of crowdfunding financing. For example, financial statements are required to be prepared and disclosed, with varying levels of detail depending on the size of the offering. For instance, the issuer’s financial statements are required to be reviewed by an independent public accountant (for offerings more than $535,000), a requirement that is counter-productive since it necessarily involves high expenses before any money is even raised (and for an issuer that usually has limited, if any, historical operations, by definition).

With respect to Reg A+ offerings, data similarly shows that they have not been popular among investors. Additionally, many companies that went public on an exchange following a Reg A+ offering have seen their shares fall afterwards. Some point out that the reason for this decline is that these offerings require only limited disclosures, which could make the issuer’s stock subject to easy manipulation and price drop. As a consequence, institutional investors have indicated that they have avoided these types of offerings. To address this issue, the SEC in July 2019 approved a decision by NASDAQ to toughen the Reg A+ standards for companies using this vehicle to go public. Time will tell whether this will have the intended effect.

On the other side, many issuers prefer Rule 506 over Reg A+ offerings because there are no mandatory disclosure provisions when offers and sales are only made to accredited investors, thereby reducing the time burdens and costs of the securities offerings. Additionally, there is no dollar limit for Rule 506 offerings while Reg A+ offerings are capped in two Tiers, adding another limitation to a financing vehicle that was advertised as being highly flexible.

2. **SEC’s Responses**

The new SEC plan to try and make Regulation crowdfunding and Reg A+ more attractive is largely focused on raising offerings caps. For Regulation crowdfunding, the SEC proposed raising the $1.07 million limit to $5 million and removing certain personal investment limits. But will it be enough? Regulatory crowdfunding is deeply perceived by sophisticated entrepreneurs as a bad way to raise capital: it is too complicated, too expensive, and requires substantial effort for little funding. The problem may actually be beyond the powers of the SEC. For example, many of the costly disclosure requirements of Regulation Crowdfunding were required by the JOBS Act itself rather than having been imposed by SEC rulemaking. Attempts have been made in Congress to pass Crowdfunding 2.0 to eliminate some of these requirements, but these efforts have not been successful to date.

For Reg A+ offerings, the main changes proposed by the SEC also consist of raising the Reg A+ caps from $50 million to $75 million for Tier 2 offerings, and from $15 million to $22.5 million for Tier 1 offerings. Though these changes might convince some new issuers to use Reg A+, the real issue with Reg A+ seems to be more the lack of a resale market that has good visibility and liquidity. This has developed because, among other things, the number of small investment banks that have
historically supported these types of offerings has substantially dwindled since 80s because of consolidation in the banking industry. It is unlikely that the government would intervene to support the creation of new small investment banks. There are a number of potential solutions that have been proposed that are in the control of government and financial markets. For example, a new stock exchange could be developed that (like NASDAQ portrayed itself to be in the 90s) focuses on emerging growth companies and Reg A+ offerings.

The real solution to the current underutilization of certain exemptions to the federal securities registration requirements is to develop exemptions that really address perceived inefficiencies in the marketplace while not “throwing the baby out with the bathwater.” The “classic” Rule 506 of Regulation D is a good example of a successful exemption: clear guidelines, thoughtful requirements and flexibility in fundraising. More can be created.

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