Market Trends 2018/19: The JOBS Act

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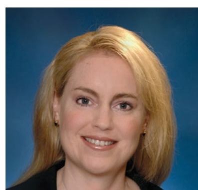

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This market trends article discusses the Jumpstart Our Business Startups Act of 2012 (112 P.L. 106, 126 Stat. 306) (JOBS Act), which was signed into law by President Obama on April 5, 2012, in response to the economic malaise following the 2009 financial crisis. Given the utility of unregistered offerings in post-recession capital formation, this article focuses on post-2012 and more recent 2018–2019 trends in small capital formation relating to JOBS Act mandated changes, including Regulation Crowdfunding (Regulation CF) for online raises up to $1.07 million, amended Regulation A for raises up to $50 million, and Rule 506(c) (17 C.F.R. § 230.506) of Regulation D permitting public solicitations to tap into unlimited quantities of capital from accredited investors. This article also examines Title I of the JOBS Act, adopted to provide access to public markets by smaller companies known as emerging growth companies.

For an overview of how these regulations compare, see Regulation D, Regulation A+, and Regulation Crowdfunding Requirements Chart.

The JOBS Act mandated that the U.S. Securities and Exchange Commission (SEC) relax historically rigid financial regulations to enable fledgling start-ups and developmental companies to advertise their ideas and solicit individuals for investments in emergent enterprises. The statute also provided an on-ramp of greater disclosure flexibility for smaller companies to transition to public companies. The economic rhetoric of the 2016 presidential election raises the question as to whether these changes made a difference. How is the JOBS Act playing out in reality? Based on economic studies conducted by the SEC, unregistered exempt securities offerings have eclipsed registered offering activity in the years following the financial crisis and passage of the JOBS Act. As of November 2019, according to the latest U.S. Department of Labor statistics, the unemployment rate is currently hovering at 3.6% with the number of unemployed persons at 5.9 million. Have securities law reforms and deregulation under the JOBS Act made a difference and, if so, how might reform of the existing regulations enhance capital formation and supplement jobs creation?

Title III – Regulation CF (Effective since May 16, 2016)

The SEC regulations under Title III – Crowdfunding, also known as the "Capital Raising Online While Deterring Fraud and Unethical Non-Disclosure Act of 2012" or the "Crowdfund Act," became effective on May 16, 2016. In June 2019, the Staff of the SEC released its three-year findings on the capital formation and investor protection aspects of Regulation CF (2019 Reg CF Report). The study captured data between May 2016 and December 2018, estimating that based on exit reporting 29 offerings had raised the full $1.07 million, with only three issuers reporting a raise of more than $1.07 million, in two or more offerings. The numbers continue to be relatively modest. It is possible that Regulation CF may become a more useful source of capital for issuers seeking start-up or bridge capital from "the crowd"—retail investors—when a sufficient critical mass of accredited investors eligible to invest under other provisions of the securities laws is not available. During 2018, the third calendar year for Regulation CF (effective since May 2016) publicly available studies report an average raise of $270,996

for the Regulation CF issuer with a success rate exceeding the success rate of issuers seeking venture capital funding. Touted by some as the best option under the JOBS Act for equity fundraising by pre-revenue ventures, the Regulation CF rules allow investors to invest amounts of as little as $100 and provide start-ups an option in the "zone of death" after "friends and family" capital and internal resources are expended. Entrepreneurs note, anecdotally, that preparation for the crowdfunding launch should begin well in advance of internal resources being exhausted. In addition to creating new channels to raise capital, the intent was to open investment avenues for new, first-time investors.

The JOBS Act also designed a new kind of financial intermediary to foster the new capital-raising initiatives. Although the term "crowdfunding" has been used for several years colloquially (in the real estate industry, especially, to refer to the way real estate platforms raise capital by giving non-private equity investors access to deals), these platforms, most of which have an online presence, have raised capital under the exemption provided by Rule 506(c) of Regulation D under the Securities Act of 1933, as amended (Securities Act). Once this long-anticipated regulation was adopted, start-up companies were permitted to tap funds up to $1.07 million in reliance on Section 4(a)(6) (15 U.S.C. § 77d) of the Securities Act during a 12-month period. The new structures operate separately from many existing processes. An issuer is not required to aggregate amounts sold under other non-crowdfunding offerings during the preceding 12-month period when calculating quantities that may be sold in a Regulation CF offering. For further information on crowdfunding, see Crowdfunding Regulations and Market Trends 2016/17: Crowdfunding.

Funding Portals Intermediaries

Regulation CF created a new category of financial intermediary, known as a funding portal. A funding portal is an entity that acts as an intermediary in a transaction involving the offer or sale of securities under Section 4(a)(6) for the account of others that does not do any of the following:

- Offer investment advice or make recommendations
- Solicit purchases, sales, or offers to buy securities offered or displayed on its platform
- Compensate promoters and others for solicitations or pay based on the sale of securities
- Hold, possess, or handle investor funds or securities

Funding portals that are not registered broker-dealers must register with the SEC. SEC rules require these registered funding portal intermediaries to:

- Provide investors with educational materials
- Take measures to reduce the risk of fraud
- Make available information about the issuer and the offering on the portal
- Provide communication channels to permit discussions about offerings on the platform
- Facilitate the offer and sale of crowdfunded securities

Broker-dealers that are members of the Financial Industry Regulatory Authority (FINRA), as well as funding portals that are registered with the SEC, are permitted to act as Regulation CF intermediaries and facilitate the sale of crowdfunded securities. Effective January 29, 2016, FINRA adopted SEC-approved FINRA Funding Portal Rules (Funding Portal Rules 100, 110, 200, 300, 800, 900, and 1200) and related forms (Form FP-NMA, Form FP-CMA, Funding Portal Rule 300(c) Form, and Form FP-Statement of Revenue), which are summarized in the FINRA Notice to Members 16-06. For further information on crowdfunding intermediaries, see Crowdfunding Intermediaries and State Intermediary Licensing Requirements for Participation in Offerings.

Portal Registrations through October 2019

Publicly available reports indicate that at the end of 2018, 61 funding portals were registered with the SEC and FINRA. More recently, the SEC's electronic filing database EDGAR reveals 49 active portals registered through October of 2019 (one portal was suspended pursuant to FINRA Rule 9553) as Funding Portals by filing their Form Funding Portal with the SEC. This is only a slight increase from the 44 portals registered in April 2018. Some of the recently registered 2018–2019 portals have focused on regional issuers, including a portal dedicated to state regulated offerings in Minnesota, Wisconsin, and Iowa (Silicon Prairie Holdings, Inc.), and industry-specific portals, including one dedicated to start-ups in the cannabis and hemp industry (Fundanna Crowdfunding). Industry analysts continue to view Regulation CF as maintaining steady-growth with potential, although in need of regulatory reforms to protect investors and verify information provided. See Report: Reg CF Offerings Top $300 Million in Total Funding, 2000+ Campaigns Funded, Crowdfundinsider.com (October 30, 2019). The portals WeFunder Portal, LLC; StartEngine; and SeedInvest continue to lead the industry in volume of offerings and commitments based on SEC filings. The consensus among industry insiders is the potential growth of this financing option for start-ups has been stymied due to an unreasonably low aggregate funding cap on capital raised during a 12-month period when considering the burdens of the regulation and the prohibition on special purpose vehicles for purchases.

Form C Disclosures – Jobs Creation and Top Industries

Form C reports and amendments filed with the SEC have been compiled by industry publication and leading analyst Crowdfund Capital Advisors in its report "The 2018 State of Regulation Crowdfunding" (2018 Reg CF Report). The reports reveal a total of 634 Regulation CF offerings filed with the SEC through the end of December 31, 2018. The report indicates that 172 issuers filing annual reports reported creating a total of 498 jobs between their annual report date and the prior year. On average, these firms created 2.9 jobs. The below sets forth the current top 15 industries by deals and commitments (quantified by number of campaigns) as compiled by CCLEAR Dashboard through November 15, 2019:

- Application Software (254)
- Beverages – Alcoholic (139)
- Personal Services (109)
- Entertainment (137)
- Consumer Capital (127)
- Restaurants (132)
- Computer Hardware (67)
- Real Property (53)
- Autos (52)
- Manufacturing (51)
- Medical (37)
- Advertising (48)
- Industrial (23)
- Utilities (36)
- Banking (60)

Regulation CF Securities Offered

The 2019 Regulation CF Report found that equity offerings were the most-often filed type of offerings through the end of 2018 (427 transactions), with the SAFE (Simple Agreement for Future Equity) offered in 287 additional transactions. A SAFE is not equity or a convertible note but a derivative instrument that promises the investor an equity stake in the company sometime in the future conditioned on whether there is an initial public offering or other liquidity event. The SAFE does not typically offer an interest payment or contain a maturity date. Debt offerings filed through the end of 2018 totaled 108 transactions, with other types of securities offered including convertible debt (106), preferred stock (105), and revenue sharing interest securities (98). In addition, several offerings for tokenized securities or initial coin offerings (Security Token Offerings or STOs) have been filed to date utilizing derivative securities such as the SAFT (Simple Agreement for Future Tokens), an arrangement closely related to the SAFE and popularized in the crypto-asset finance sector during 2017. The type of security offered may have bearing on potential investor risk. The 2019 Regulation CF Report indicates that crowdfunding investors may generally have more limited voting rights and less control because of the use of debt, SAFE securities, and classes of equity securities that lack voting rights.

Interpretations in Crowdfunding Issuer Communications and Advertising

The Regulation CF advertising rules may not be intuitive for many business persons and lawyers. Rule 204(a) (17 C.F.R. § 227.204) of Regulation CF provides that issuers and persons acting on the issuer's behalf may advertise the terms of the Section 4(a)(6) offering, referred to as "general solicitation." General solicitation was not previously permitted for exempt private offerings. The staff of the Division of Corporation Finance of the SEC (the Staff) has clarified that advertising by an issuer may extend beyond the confines of the Rule 204(b) Tombstone-like notice, provided that the issuer's advertisement does not contain terms of the offering. In that event, the issuer is not restricted in providing notice of its offering through social media or other mediums, subject to anti-fraud rules. See Compliance and Disclosure Interpretation (C&DI) Question 204.03 released on May 13, 2016. The terms of the offering are defined in the rules to include information about the securities including the type of security and the duration of the offering. For an overview of permitted issuer communications in general in registered offerings, see When is a Communication an Offer of Securities? Chart.

Recent Interpretations in Crowdfunding Issuer Disclosure and Reporting

During 2019, the Staff published an additional interpretation addressing interests in qualified opportunity zones. The Staff Statement on Opportunity Zones: Federal and State Securities Laws Considerations stated that such interests are likely to constitute securities within the meaning of the federal securities laws.

C&DI Question 204.05 addresses a concern that capital-raising options in qualified opportunity zones are limited for local residents in opportunity zone communities who may not qualify as an accredited investor. The question clarifies that a Regulation CF offer and sale to nonaccredited investors could be used in conjunction with a Rule 506(c) offering to accredited investors. The interpretation further provides that an issuer, with the assistance of legal counsel who can structure the offerings to comply with the federal

securities laws, may structure an offering under Rule 506(c), utilizing general solicitation, in a manner such that the offering would not be integrated with a Regulation Crowdfunding offering as long as any general solicitation and advertisement for the Rule 506(c) offering (i) do not include the terms of the Regulation Crowdfunding offering, or (ii) if such advertisement also complies with the requirements of a Regulation Crowdfunding offering (including necessary legends and restrictions on the general solicitation under Regulation Crowdfunding).

Intermediary Compensation

The 2019 Reg CF Report aggregated data on intermediary compensation ranges over the brief history of Reg CF. Based on an analysis of the Form C filings from May 2016 through December 31, 2018, most Regulation CF intermediaries, including both funding portals and broker-dealers, acting as intermediaries, receive a percentage fee paid in either cash or securities, or a combination of both, conditioned on offering completion. On average, the intermediary compensation reported in Form C filings ranged from 0.1% to 10% of the total proceeds of the offering, with the intermediary, in about 23% of the offerings reported, requiring the issuer to reimburse it for out-of-pocket expenses. In about 37% of the offerings the intermediary received securities of the issuer as compensation, and in those cases, the average amount was 2.9% of the offering proceeds.

The average intermediary compensation was higher when charged by broker-dealers. The average fee that broker-dealer affiliated intermediaries charged was 7.1%, as compared with the fee that funding portals charged of 5.5%. Broker-dealer affiliated intermediaries have been more likely to take securities as part of their compensation package as compared with funding portals—with broker-dealers granted securities in 88% of their campaigns contrasted with 29% for funding portal campaigns. The additional services that may be rendered to issuers include the preparation of crowdfunding materials and Regulation CF filings.

Trending Finance Structure of Title III Deals

Trending in Regulation CF transactions during 2018–2019 are an issuer's use of revenue sharing notes and arrangements whereby the start-up agrees to pay a crowdfunding investor a percentage of the company's periodic revenues until a target return is achieved as opposed to issuing common stock or other equity instrument. Evidence suggests that the Regulation CF "crowd" has become increasingly savvy, and is more highly receptive to the revenue sharing note providing an immediate incentive for the investment rather than, as in the past, relying on management to build a company to either pay dividends, distributions, or become an attractive acquisition target. Not only can the revenue sharing note (in lieu of equity) address the investor's liquidity and exit concerns, it may reduce complexity for the company by avoiding additional equity owners and simplifying ownership structure, and retaining voting, and governance of the business by the existing equity owners. The revenue sharing arrangement may be structured to address the variable revenues of the business in that when revenue streams are higher, the investor receives more cash flow and, in the periods, when revenues are slower, the investor payments are reduced accordingly to avoid undue strain on the early stage business. In some situations, including a consumer services business, the revenue sharing instrument may incentivize the investor to patronize and advocate for the business to increase the customer base and enhance the revenue performance of the business.

Regulation CF Inflation Adjustments

Effective April 12, 2017, the SEC adopted new rules amending Regulation CF and Form C to adjust dollar amounts to inflation. Under the amendments, the rounded inflation adjusted maximum amount an issuer can sell under Regulation CF in a 12-month period increased from $1 million to $1.07 million. Similarly, the adjusted maximum amount that can be sold to an investor under Regulation CF in a 12-month period is now increased from $100,000 to $107,000. Finally, the adjustments increased the cap on the aggregate value of securities permitted to be sold to an investor if the investor's annual income or net worth is less than $107,000 from $2,000 to $2,200. The dollar amounts are statutorily required to be adjusted by the SEC once every five years for changes in the Consumer Price Index for All Urban Consumers.

State of Regulation CF

The 2019 Reg CF Report indicates a slow steady adoption of Reg CF by early stage companies with securities crowdfunding campaigns in all 50 U.S. states except Montana, North Dakota, Nebraska, Kansas, and Iowa. California is the leading jurisdiction for start-up businesses engaged in crowdfunding with an estimated 574 campaigns and $112.13 million in funding commitments, followed by New York (224 campaigns), Texas (156 campaigns), and Florida (127 campaigns). More recent 2019 news reports that as of November 22, 2019, North Dakota is now the only state with no reported Regulation CF offering. Specifically, Regulation CF companies have been small, and the median issuer has been a start-up incorporated approximately two years before the offering with about three employees with total assets of an estimated $30,000 and cash on hand of $4,000, while about half of the issuers report being in the pre-revenue phase. Notwithstanding the short duration to

observe activities (less than three full years of study since the Reg CF adoption), according to the report, there appears to be little enforcement activity against issuers of securities and intermediaries in the crowdfunding space (contrasted with earlier fears that Reg CF financings would or could be disproportionately fraught with fraudulent activity).

Notably, the data gathered to date indicates an average raise of $250,635 by offering with approximately $300 million raised to date, although the most prominent and vocal industry advocates and supporters predict, assuming legislative reforms increasing the issuer cap from $1 million to $20 million or other more substantial size, that the U.S. market will reach approximately $1 billion in funding during the next five years, based on the crowdfunding financing growth rate in analogous non-U.S. international markets. The data additionally suggests that few Regulation Crowdfunding participants have used the Regulation D offering market in the previously, suggesting that Regulation CF, now in the early stages of the regulation, tends to bring new first-time issuers to the capital markets (about 13% have undertaken a Regulation D offering in advance of the Regulation CF financing). The data indicates that only an estimated 105 issuers returned to the Regulation CF market for a follow-on offering.

In terms of potential reforms to Regulation CF, the 2018 Small Business Forum participants to the SEC hosted Government-Business Forum on Small Business Capital Formation made the following recommendations in the Final Report of the SEC, published June 2019:

- Accredited investors should be permitted to invest any amount they want in Regulation Crowdfunding offerings, provided the accredited status of the investor is verified. Removing the individual accredited investor limits would make Regulation Crowdfunding offerings a more attractive investment vehicle to accredited investors and make it easier for offerings to reach their maximum offering goals.
- The limits for all investors should be raised. Nonaccredited investors want to invest more in offerings and should be free to do so. This will only help the market grow as it allows more individual investments into the marketplace.
- The advertising rules and restrictions should be loosened to allow issuers to more effectively market their projects. It is very difficult for issuers to understand the burden of the advertising rules, and the rules run counter to the intent of the law: to promote the democratization of investing. The issuers should be allowed to speak more directly to the terms of the offering.
- Recommended portals be allowed to receive securities of the issuer as compensation having different terms than the securities of the issuer received by investors in the offering (e.g., allow portals to receive warrants as compensation with different terms than the warrants sold to investors in the offering) and also allow portals to co-invest in the offerings they list.
- Recommended the SEC lead a joint effort with FINRA to provide clear guidance to participants in Regulation Crowdfunding offerings.
- Rationalize Regulation Crowdfunding requirements for debt offerings and small offerings under $250,000, by limiting the ongoing reporting obligations to actual noteholders (not to the general public) and scaling regulation to reduce accounting, legal, and other costs that now are relatively inelastic, regardless of the size of the offering.

The participant recommendations were developed by the 2018 Forum participants. The rationales and detailed explanations for the recommendations are beyond the scope of this article and are included in this article only to provide context to the data points contained in this article and to outline potential future trends. It is important to understand that while the SEC conducts the forum, it does not develop, endorse, or modify the recommendations presented in the report.

TITLE IV – Regulation A+ (Effective since June 2015)

Increased Issuer Activity following Amendments to Regulation A under the JOBS Act

In the four-year period following the effectiveness of the Regulation A+ rules, companies are taking advantage of the exemption from securities registration afforded by Regulation A+ at a rate surpassing that under the prior Regulation A regime. The prior Regulation A had an offering cap of $5 million, which was perceived as cost inefficient, according to the November 2016 study prepared for the SEC's Division of Economic and Risk Analysis (DERA). See A. Knyazeva, Regulation A+: What Do We Know So Far? (November 2016) (the Regulation A+ Study). Although this study has not been updated as yet, it can be illustrative of the trends seen in the amended Regulation A filings for the first portion of the period in which it has been in effect. In contrast, Regulation A+ has two tiers of offerings, with the higher level permitting offerings of up to $50 million.

Size of Regulation A+ Deals

According to the DERA economic analysis Capital Raising in the U.S.: An Analysis of the Market for Unregistered

Securities Offerings, 2009–2017 (DERA Capital Raising Study), for the period between May 16, 2016 through December 31, 2017, Tier 2 Regulation A qualified offerings (with 128 qualified offerings) comprised approximately double the number of Tier 1 offerings (with 57 qualified offerings). As expected, a typical Tier 2 issuer was seeking to raise a larger amount. The aggregate amounts sought by the Tier 2 issuers for all offerings during the period was $3.7 billion with a total of $542.7 raised during the period. By comparison, the aggregate amount sought by the Tier 1 issuers for all offerings during the period was $488.1 million with a total of $126 million raising during the period. For further information on the respective tiers in Regulation A+, see "Regulation A-Plus" Tier 1 and Tier 2 Offerings Summary Chart.

Regulation A+ Offering Industry Distribution

The DERA Capital Raising Study further provided that the top industries filing Regulation A offering statements since effectiveness up to the date of the study included:

- For Tier 1:
  - Business Services (19.3%)
  - Depositary Institutions (19.3%)
  - Non-depository Credit Institutions (12.3%)
  - Real Estate (10.5%)
  - Motion Pictures (5.3%)
- For Tier 2:
  - Investing (13.6%)
  - Real Estate (12.8%)
  - Business Services (12.0%)
  - Transportation Equipment (8.8%)
  - Non-depositary Credit Institutions (4.8%)

Timeline

The Regulation A+ Study's sampling of qualified filings revealed that the length of the SEC qualification process for new Regulation A offerings was a median time of 78 days from initial public filing to qualification as compared to an average of 228 days to qualify between 2002 through 2011 prior to the JOBS Act amendments. Perhaps not surprisingly, Tier 2 offerings were generally associated with a longer timeline than Tier 1 offerings, according to the Regulation A+ Study.

The author's experience currently is a general estimated time frame of 65–75 calendar days from the initial filing to qualification for Tier 2 offerings.

2019 Progress Update for Regulation A+

On December 19, 2018, the SEC announced that it adopted amendments to 17 C.F.R. § 230.257 (Rule 257) to make 1934 Act reporting companies eligible to utilize Regulation A. In addition, with respect to Tier 2 offerings, the amended rule provides that such issuers would be deemed to have met the periodic and current reporting requirements under Regulation A if they have otherwise complied with the reporting requirements of the 1934 Act.

To maximize the effectiveness of Regulation A, the 2018 Small Business Forum participants to the SEC hosted Government-Business Forum on Small Business Capital Formation recommended the following as summarized in the Final Report of the SEC.

The recommendations requested guidance for market-participants including broker-dealers, transfer agents, and clearing firms regarding Regulation A securities including the ability of a funding portal to participate in a Regulation A offering. The forum committee report included specifically the requests for the SEC to consider revisions to Regulation A, as follows:

- Mandate blue sky preemption for secondary trading of Regulation A Tier 2 securities
- Allow at-the-market offerings
- Implement rules allowing all reporting companies to use Regulation A
- Increase the maximum offering amount in any 12-month period from $50 million to $75 million for Regulation A Tier 2 offerings
- Consider overriding advance notice requirements of state regulators in Regulation A offerings and limiting state filing fees for these offerings
- Require any portal that is in the business of facilitating Regulation A offerings to register as a broker-dealer and comply with requirements similar to the requirements for intermediaries under Regulation Crowdfunding, and adhere to disclosure requirements including required disclosure of compensation and the amount thereof
- SEC recognition of quick response (QR) codes in lieu of a hyperlink to a prospectus or offering circular after the offering has gone effective or been qualified
- Platforms that offer Regulation A securities offerings should be regulated like other portals, including adhering to FINRA guidelines –and–
- The SEC should enforce Regulation SHO and Regulation T for all IPOs, including Regulation A offerings

Title II – Regulation D, Rule 506(c) (Effective since September 2013)

Rule 506(c) under Title II of the JOBS Act allows an issuer to solicit investors and advertise its offering, provided the investment opportunity is confined to accredited investors. Offerings under Regulation D were previously required to be conducted without any general solicitation of investors. Subsection 506(c) changes that requirement. An offering may engage in general solicitation of investors if the securities are sold to only those investors who can affirmatively demonstrate their "accredited investors" status. For further information, see JOBS Act Impact on Private Placement Transactions. By some economists' accounts, the 506(c) offering continues to be underutilized by companies who in some instances would like to continue to rely on their preexisting relationship networks to complete an offering. According to the economic analysis Capital Raising in the U.S.: An Analysis of the Market for Unregistered Securities Offerings, 2009–2017, amounts reported raised under Rule 506(c) in the period immediately following effectiveness of the rule remained a small fraction of the total (4%; $255 billion) of the capital reported raised pursuant to Regulation D during that same period, suggesting that most issuers of unregistered securities are not yet seeking investors through general solicitation and general advertising. See Bauguess, Rachita, Gullapalli, and Ivanov, "Capital Raising in the U.S.: An Analysis of the Market for Unregistered Securities Offerings, 2009–2017" (August 2018), at page 2 (the Regulation D Study).

The Regulation D Study found that issuers with preexisting sources of financing or intermediation channels may not yet need the flexibility provided by Rule 506(c). Additionally, issuers may become more comfortable with market practices as they develop over time, including among other things, legal certainty over what constitutes general solicitation. Further, there are concerns about the levels of verification of the accredited investor status of purchasers. Some anecdotal evidence exists that issuers also fear the perception that use of general solicitation signals to the market that the company lacks a preexisting network of sophisticated investors and does not have favorable financing options. For further information on Rule 506, see Rule 506 General Solicitation and Startup Capital-Raising and Regulation D Components. There may also be some concern that investors may push back on the information required to be provided under the new provision.

Increased Use of Rule 506(c) Trending

Private capital markets in the United States and worldwide sought an unregulated financing option during 2017 through initial coin offering launches of a new asset class: tokens, digital "coins," and tokenized securities. Many technology start-ups were fueled through such unregulated offerings during late 2016 and 2017, financing over $4 billion in early stage ventures. A limited portion of these token financings were also conducted under Regulation D, Rule 506. Regulation D capital funding of token offerings has continued during 2018 and 2019 given the SEC's clear guidance that it has jurisdictional authority in the digital assets financing because certain of these offerings constitute securities offerings and must either be registered or qualify for an exemption. During 2018 and 2019, security token launches were rebranded from the earlier 2017 initial coin offering or ICO to evidence their regulatory compliance and migrated to well-known crowdfunding portals hosting the security token and digital asset offerings and issuing digital assets through the Rule 506(c) exemption. The digital asset rebranding occurred in the wake of enforcement activities of the SEC and state regulators; however, many security token offerings have continued to include general solicitation and advertising to the public.

Pooled investment fund issuers, including hedge funds, venture capital funds, private equity funds, and other pooled investment funds (Fund Issuers), have increasingly utilized the Rule 506(c) exemption in the period covered by the Regulation D Study (September 23, 2013–December 31, 2017) with the total cash raised in the 506(c) market, 75% of the capital was raised by Fund Issuers, compared with non-Fund Issuers at 25%. Noteworthy, the study points out, that although the non-fund issuers raised significantly less than Fund Issuers in the Regulation D market, non-fund issuer raises account for the majority of the all new Form D offering filings.

The Regulation D Study revealed that for non-fund issuers, financial companies and technology industry (including computers, other technology, and biotechnology) were the most active industries in the Rule 506(c) market. Other industries most often represented in the non-fund issuer market include commercial, other real estate, and residential industries.

In view of the increasing market in online platform fundraising, accredited investors continue to be highly coveted as online portal communities expand and platforms and portal communities have become specialized by affinity groups, social causes, and local and regional geography

as well as industry sector, with real estate financing and real estate fund portals becoming increasingly diverse and competitive during 2018–2019.

Title I – IPO On-Ramp

The provisions of Title I of the JOBS Act created a category of emerging growth companies or issuers with less than $1 billion (currently $1.07 billion) in annual gross revenue during their most recently completed fiscal year (EGCs). Title I, entitled "Reopening American Capital Markets to Emerging Growth Companies," was designed to revitalize IPOs by smaller issuers by reducing various disclosure and compliance requirements for EGCs during a public offering and for up to five years thereafter. EGCs are provided with a phase-in period of up to five years to comply with the more burdensome disclosure and accounting requirements of federal securities laws. For further information, see Emerging Growth Company Guide for Capital Markets, Top 10 Practice Tips: Emerging Growth Companies, Emerging Growth Company versus Smaller Reporting Company Comparison Chart, and IPO Requirements for Emerging Growth Companies Checklist. IPO companies have varied with their use of the EGC disclosure flexibility.

Under the JOBS Act inflation adjustments discussed above, the SEC will index to inflation the annual gross revenue cap amount used to determine EGC status every five years, with the next adjustment scheduled for 2022.

IPO Activity Post-JOBS Act

The data for the IPO market shows that during 2018, 190 IPOs were priced raising $47 billion, an increase of 32% in proceeds as compared with 2017, a high point over the prior four years although the fourth quarter of 2018 ended the year with uncertainty following a global sell-off leaving a negative aftermarket return of -2%. Biotechs continued to be the star performers in 2018, with 10 IPOs in excess of a billion dollars and a public offering using an unusual direct listing. In addition, an influx of Chinese issuers accessed the U.S. capital markets. See Renaissance Capital, US IPO Market 2018 Annual Review (January 2, 2018) (the 2018 Renaissance Report).

The noticeable decline of publicly listed U.S. companies received more attention this year and is the catalyst for what commentators have viewed as a deregulatory trend within the SEC both in terms of rulemaking and enforcement activity for public companies. As an example, this includes a recent proposal to eliminate a Sarbanes-Oxley Act driven internal control requirement for pre-revenue companies, a compliance requirement that auditors attest to effectiveness of the company's internal controls. In its October 2017 report to the president of the United States on the state of the capital markets (the 2017 Treasury Report), the U.S. Department of the Treasury reported that while the number of U.S. public companies has declined by half since 1996, other developed countries have not experienced the same trend and have instead experienced increases. Similarly, the U.S. IPO activity has trended in sharp decline following 1996, although some data supports a short-term bump in performance following passage of the JOBS Act.

SEC Chairman Jay Clayton, the Council of Institutional Investors, and the U.S. Chamber of Commerce released in-depth studies during 2017 addressing this troubling trend and citing continued burdensome regulatory regimes causing issuers to resist or postpone entrance into the public markets. Some of the studies presented proposals for JOBS Act reforms to stimulate the U.S. IPO markets, included extending the "on-ramp" accommodations of the JOBS Act from five years to ten years for all EGCs and making the JOBS Act on-ramp available for all companies seeking an IPO for five years, regardless of whether they meet the definition of an EGC.

IPO Industry Insights

According to the Renaissance Capital U.S. IPO report of Q3 2019, healthcare and technology dominated the IPO market and made up 62% of the IPOs with biotechs and large U.S. technology companies leading the charge. At least two high-profile much publicized IPOs stalled on their debut. During the quarter, 39 offerings raised a total of $10.8 billion which is a decline by 25% in IPOs compared the same period of third quarter 2018. Other sectors with IPOs during the third quarter included consumer-driven companies: a cannabis grower, an exercise bike company, an education group, and a restaurant chain.

JOBS Act Recalibration Now Recommended by the Treasury Department

The 2017 Treasury Report signaled that amendments to the JOBS Act were on the horizon and recalibration may be supported in the short term by the current SEC Commissioners. The report notes that:

> [A]fter a few years of experience following the JOBS Act, it is time to take another look at how these tools can be improved. Treasury's recommendations also seek to maintain the efficacy of the private equity markets, which will continue to be important for some companies and entrepreneurs. These recommendations include maintaining an appropriate regulatory structure for finders, expanding the range of eligible investors, empowering investor due diligence efforts, and modifying the rules for private funds investing in private offerings.

Given opportunities have diminished for investors in the public markets and the trend of companies waiting to go public, in the vein of deregulation, the following reforms have been proposed during 2019:

- Expansion of the pool of companies that can use Regulation A to raise funds, under the FAST Act Modernization and Simplification of Regulation S-K, Final Rule, Mar. 20, 2018 (see "2019 Progress Update for Regulation A+" above)
- A proposal expanding on the JOBS Act Regulation A relaxations, which would allow all issuers to test the waters by communicating with potential investors to gauge their interest in a contemplated registered securities offering
- Revisions to the auditor independence requirements –and–
- Expanding the number of companies that qualify as smaller reporting companies and thus reduced disclosure and reporting requirements

Market Outlook

Additional rulemaking reforms will likely be proposed by the SEC in 2020 to address the declining number of public companies as well as to address small capital formation issues and difficulties start-ups continue to face in competing in the capital markets. The SEC will continue to modernize the regulatory framework around exemptions from registration and the ability to generally solicit investors and advertise the salient points of an offering. The SEC's 2020 proposals are likely to include long-awaited changes to relax the definition of an accredited investor, to take the JOBS Act rulemaking another step.

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Rebecca G. DiStefano concentrates her diverse practice in securities regulation, corporate finance, and mergers and acquisitions law and serves on the Greenberg Traurig Blockchain Task Force. Rebecca counsels public and private companies in areas including private placements, registrations, Regulation A+ qualifications, and crowdfunding under the JOBS Act of 2012 and the Securities Act of 1933. Related to these transactions, she advises companies and their boards regarding attendant corporate governance best practices, fiduciary duties, continuing disclosure and reporting requirements of Regulation A+ and the Securities Exchange Act of 1934, as well as helping clients navigate cross-border and blue sky issues, secondary trading issues and the initial and continued listing of corporate securities. Additionally, she structures and organizes for clients non-U.S. regulated investment vehicles including private equity funds, funds of funds, and hybrid funds. Rebecca regularly represents her clients before the U.S. Securities and Exchange Commission and FINRA and is experienced structuring ESOP transactions and counseling ESOP-owned companies and ESOP trustees (both prior to and subsequent to the ESOP purchase).

Rebecca frequently speaks and authors on recent trends in U.S. Capital Markets, post-JOBS Act financial regulation, and related Blockchain & Cryptocurrency developments. Since 2013, she has been devoted to improving lives of children and adults diagnosed with diabetes through JDRF advocacy in Florida and in Washington D.C. and is a member of the JDRF Ride-to-Cure Team. Rebecca has been listed in The Legal 500 United States, 2009, and The Best Lawyers in America, for Corporate Law, from 2016-2019.

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