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How to Crowdfund and Not Fall Flat on Your Face: Best Practices for Investment Crowdfunding Offerings and the Data to Prove It

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HOW TO CROWDFUND AND NOT FALL FLAT ON YOUR FACE: BEST PRACTICES FOR INVESTMENT CROWDFUNDING OFFERINGS AND THE DATA TO PROVE IT

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I. INTRODUCTION

Regulation Crowdfunding ("Reg CF") has already celebrated its first anniversary.[1] After a frustratingly long delay during Securities and Exchange Commission (SEC) rulemaking for the JOBS Act's most modern securities fundraising technique,[2] issuers may now tap the Internet's vast populace to raise money. By many measures, the law is working—existing small businesses and new startups alike are getting the jumpstart they need.[3] As an added benefit, the companies funded by investment crowdfunding also seem to be creating the kinds of jobs (if perhaps not yet in the desired numbers) originally envisioned by lawmakers.[4] It seems that, barring some shift in the legislative agenda of Congress, federal investment crowdfunding is here to stay.[5]

1. *See* Crowdfunding, Securities Act Release No. 33-9974, Exchange Act Release No. 34-76324, 80 Fed. Reg. 71,388, 71,388 (Nov. 16, 2015) (to be codified at 17 C.F.R pts. 200, 227, 232, 239, 240, 249, 269, and 274) [hereinafter Regulation Crowdfunding] ("The final rules and forms are effective May 16, 2016 . . . ."). Portal registration has been open since January 29, 2016. *Id.*

2. *See* Samuel Guzik, *JOBS Act Crowdfunding Begins on May 16, 2016: Don't Get Busted for Solicitation!*, CROWDFUND INSIDER (Mar. 28, 2016, 4:00 AM), https://www.crowdfundinsider.com/2016/03/83470-jobs-act-crowdfunding-begins-on-may-16-2016-dont-get-busted-for-solicitation/ ("Though Congress dictated that this task be completed by the end of 2012, the SEC missed the mark by nearly three years."); *see also* Jumpstart Our Business Startups Act, Pub. L. No. 112-106, 126 Stat. 306, 320 (2012) [hereinafter JOBS Act] (requiring rulemaking by the SEC "not later than 270 days after the date of enactment").

3. *See* Larry Alton, *Does Crowdfunding for Startups Actually Work?*, PURCH, https://www.business.com/articles/does-crowdfunding-for-startups-actually-work/ (last visited Mar. 31, 2017).

4. *See* Sherwood Neiss, *Here's How Regulation Crowdfunding Performed in 2016*, VENTUREBEAT (Jan. 11, 2017, 5:05 PM), http://venturebeat.com/2017/01/11/heres-how-regulation-crowdfunding-performed-in-2016/ (reporting a job creation rate of 2.2 jobs per funded company, often in "underserved communities").

5. *See id.* (advocating for the incoming administration to promote crowdfunding, especially as an economic booster since many investors fund local projects). It seems unlikely that the current Republican-controlled Congress will drastically alter the JOBS Act, a measure that originally passed with overwhelming Republican support. *See* Pete Kasperowicz, *House Approves JOBS Act in 390-23 Vote*, THE HILL (Mar. 8, 2012, 6:02 PM), http://thehill.com/blogs/floor-action/house/214979-house-passes-jobs-act-sends-to-senate. In fact, the Crowdfunding Enhancement Act is already under consideration in an attempt to further enable online capital raising via crowdfunding. *See* Crowdfunding Enhancement Act, S. 1031, 115th Cong. (2017), https://www.congress.gov/bill/115th-congress/senate

At the same time, many states have also waded into the fray with their own crowdfunding solutions.[6] In fact, several states had operational investment crowdfunding systems months and even years before the federal government.[7] Many of the same benefits—job creation, driving community entrepreneurship, survival of small businesses—seem to be trickling down in the intrastate models as well.[8] The probability exists, especially as the federal model builds steam and gains even broader support across state legislatures, that state-level investment crowdfunding will also be around for the long haul.[9]

While there have been comparatively few Reg CF offerings to date (with relatively small offering amount aggregates, at least as

-bill/1031; *see also infra* Part V.

6. *See, e.g.*, MNvest Registration Exemption, MINN. STAT. § 80A.461 (2016). For a list of intrastate crowdfunding statutes current through November 16, 2016, see N. AM. SEC. ADM'RS ASS'N, NASAA INTRASTATE CROWDFUNDING UPDATE (2016) [hereinafter NASAA INTRASTATE OVERVIEW], http://nasaa.cdn.s3.amazonaws.com/wp-content/uploads/2014/12/NASAA-Intrastate-Crowdfunding-Update-111616.pdf.

7. NASAA INTRASTATE OVERVIEW, *supra* note 6, at 3.

8. *See id.* at 5 (listing a variety of businesses and industries that use intrastate crowdfunding).

9. As contrasted with federal Reg CF, legislative changes will be almost necessary in order for intrastate crowdfunding statutes to maintain their efficacy. Most intrastate crowdfunding models are tied to the federal intrastate offering exemption under 15 U.S.C. § 77(c)(a)(11) (2016). *See* N. AM. SEC. ADM'RS ASS'N, INTRASTATE CROWDFUNDING LEGISLATION (2016), http://nasaa.cdn.s3.amazonaws.com/wp-content/uploads/2014/12/NASAA-Crowdfunding-Index-11-16-2016.pdf. The SEC recently made changes to the Rule 147 safe harbor for intrastate offering advertising and solicitation and introduced a completely new exemption dubbed Rule 147A. *See* Exemptions to Facilitate Intrastate and Regional Securities Offerings, Securities Act Release No. 33-10238, Exchange Act Release No. 34-79161, 81 Fed. Reg. 83,494 (Nov. 21, 2016) [hereinafter Final Rules 147/147A]. State laws based on compliance with section 3(a)(11) of the Securities Act of 1933 *and* Rule 147 will need to be amended in order to take full advantage of the revisions. For a deeper analysis of the problem created by mandatory compliance with section 3(a)(11) and old Rule 147, see Timothy M. Joyce, *1000 Days Late and $1 Million Short: The Rise and Rise of Intrastate Equity Crowdfunding*, 18 MINN. J.L. SCI. & TECH. 343 (2017).

compared to other options like Regulation A+[10] and Regulation D[11]), there have been enough offerings to amass sufficient data[12] from which to draw some meaningful conclusions about the likely causes of the success or failure of an offering. And some practitioners have already begun to crunch the numbers.[13] To the extent that it is possible to glean some useful guidance from previous offerings, this article attempts to synthesize the data with the authors' personal and practical experiences[14] to propose some investment crowdfunding

10. *See* J.D. Alois, *NextGen Reports on Reg A+ Market: Reviews Early Data on 131 Filings*, CROWDFUND INSIDER (Oct. 10, 2016, 4:18 PM), http://www.crowdfundinsider.com/2016/10/91066-nextgen-reports-reg-market-reviews-early-data-131-filings/ (summarizing a NextGen report on Regulation A+ offerings under Title II of the JOBS Act). "[F]or a full year between June 19, 2015 and June 22, 2016," Tier I and Tier II companies solicited a combined total of more than $2 billion. *Id.* Based on just the raw numbers of offerings, Regulation A+ seems to have somewhat similar popularity as Reg CF. *Compare id.* (reporting either 131 or 144 Regulation A+ offerings, depending on which analysis is trusted), *with* Samuel Effron, *Regulation Crowdfunding: A Six-Month Update*, JD SUPRA (Dec. 28, 2016), http://www.jdsupra.com/legalnews/regulation-crowdfunding-a-six-month-15854/ (reporting 160 Form C filings in 2016).

11. *See* Effron, *supra* note 10 ("[T]he total amount raised in Reg CF offerings in this six-month period compares very unfavorably to the amount raised in Regulation D offerings during the same period, which is close to $30 billion.").

12. Form C data is publicly available via search of the EDGAR system. *See EDGAR Search Tools*, U.S. SEC. & EXCHANGE COMMISSION, https://www.sec.gov/edgar/searchedgar/webusers.htm (last visited Mar. 31, 2017). Wefunder, one of the first registered portals under Reg CF, also keeps up-to-date tallies of Reg CF offerings. *See The Current Status of Regulation Crowdfunding*, WEFUNDER, https://wefunder.com/stats (last visited Mar. 31, 2017) (reporting 122 offerings to date, 82 of which have been successfully funded, for a total in excess of $20 million).

13. *E.g.*, *CCA Regulation Crowdfunding Indices*, CROWDFUND CAP. ADVISORS, http://crowdfundcapitaladvisors.com/cca-regulation-crowdfunding-indices/ (last visited Mar. 31, 2017); *The Current Status of Regulation Crowdfunding*, *supra* note 12; Marc A. Leaf et al., *Leading the Crowd: An Analysis of the First 50 Crowdfunding Offerings*, DRINKER BIDDLE: INSIGHTS & EVENTS (July 14, 2016), http://www.drinkerbiddle.com/insights/publications/2016/07/leading-the-crowd-first-50-crowdfunding-offerings. The Crowdfund Capital Advisors numbers inform a substantial part of the analysis in Part III, *infra*.

14. Author Zach Robins participated in the drafting of the MNvest statute in Minnesota. He practices in the area of securities law and represents clients on both the issuer and portal operator sides of an offering. Author Tim Joyce assisted Zach on one of the first crowdfunding offerings under MNvest during a 2016 summer associateship at Winthrop & Weinstine, PA in Minneapolis, Minnesota.

best practices.[15] In addition, this article suggests some best practices for potential crowdfunders in areas of offerings not easily reduced to numerical data points.[16] In the end, the authors hope to provide actionable advice to the potential crowdfund issuer and its counsel for crafting the most appropriate offering structure for a given capital raise.[17]

The article proceeds in four[18] parts: Part II provides a brief description of investment crowdfunding, as a necessary history for an uninitiated reader.[19] Next, Part III examines the publicly available data on federal crowdfunding offerings to date.[20] Then, Part IV uses the data to recommend best practices for investment crowdfunding offerings using Reg CF, including some best practices that do not submit easily to numerical data points.[21] Part V offers some next steps in the evolution of federal- and state-level crowdfunding and a brief conclusion to the article.[22]

II. REGULATION CROWDFUNDING OFFERINGS AT A GLANCE

Any evaluation of the ideal crowdfunding offering will require an understanding of crowdfunding's unique place in the panoply of securities fundraising techniques. Investment crowdfunding first emerged as one part of a comprehensive solution to free up stalled U.S. capital markets, particularly for small businesses.[23] After the catastrophic market crash in the latter part of the first decade of the twenty-first century, traditional sources of capital had dried up.[24] For the most part, the end result and purpose—the "what" and "why" of

15. *See infra* Part IV.
16. *See infra* Part IV.
17. *See infra* Part IV.
18. Note that the Postscript, *infra* Part VI, is intended as an addendum speaking to the topic of the 2017 Mitchell Hamline Law Review Symposium. The scope of the Postscript is both broader and different than the rest of the article.
19. *See infra* Part II.
20. *See infra* Part III.
21. *See infra* Part IV.
22. *See infra* Part V.
23. *See* WILLIAM MICHAEL CUNNINGHAM, THE JOBS ACT: CROWDFUNDING FOR SMALL BUSINESSES AND STARTUPS 21 (2012) ("When banks are told to reduce risk, small businesses, especially startups, are the first to see credit levels reduced.").
24. *See, e.g.*, *id.* at 23 ("Over the last ten years, the number of companies raising capital through the issuance of stock in the public securities markets has declined dramatically.").

a crowdfunding offering—are much the same as any securities offering.[25] An issuer receives money from investors for the purpose of starting, maintaining, or expanding its operations. It is in the details about market players and offering implementation—the "who," "how," and "much" of these offerings—that investment crowdfunding offers truly unique fundraising solutions. The next sections will highlight and comment upon the most important differences between crowdfunding and other federal[26] securities exemptions.

A. *The "Who": Investors and Issuers*

Where other parts of the JOBS Act focused on increasing the amount of capital available to an issuer each year[27] or freeing up publicity restrictions,[28] the main innovation embodied in Title III of the Act involved reaching a previously underrepresented type of investor on a large scale: the non-accredited investor.[29] Prior to that

25. The academic literature is rife with analysis of how investment crowdfunding fits (or does not fit) into the federal securities regulation schema. For a recent exploration of how Securities Act section 4(a)(6) and Reg CF stack up against other securities fundraising techniques, particularly Minnesota's intrastate alternative, see generally Joyce, *supra* note 9. This article will not attempt to replicate those efforts and thus assumes at least a passing familiarity with federal securities law. However, for the truly uninitiated, roughly: In the United States, the offer and sale of shares of profits based on the efforts of others is governed by securities laws, both at the state and federal levels. Issuers offering such shares must either register the shares or find an exemption. Section 4(a)(6) in Title III of the JOBS Act created an exemption for the sale of securities based on a crowdfunding model, 15 U.S.C. § 77d(a)(6) (2012), and it is with this exemption that this paper is principally concerned.

26. The most accessible crowdfunding offering data comes from federal Form C filings with the SEC. Although many states have operational intrastate crowdfunding statutes, information based on those offerings is either nonpublic or simply not large enough to warrant the drawing of many conclusions. *See* NASAA INTRASTATE OVERVIEW, *supra* note 6. Further, each state's enactment of intrastate crowdfunding differs slightly from the others; thus, a comparison would be of apples and oranges.

27. *See* JOBS Act, Pub. L. No. 112-106, 126 Stat. 306, 401–02 (2012) (Regulation A+ offering exemption for annual limit increases).

28. *Id.* § 105.

29. It is estimated that only a miniscule portion of the U.S. population qualifies as "accredited investors" for securities law purposes. *See* Devin Thorpe, *SEC Mulls Changes to Accredited Investor Standards, 18 Crowdfunders React*, FORBES (July 15, 2014, 12:32 PM), https://www.forbes.com/sites/devinthorpe/2014/07/15/sec-mulls

point, the substantial[30] pool of potential investors who did not meet the income or net worth thresholds for "accreditation" were effectively barred from participation in the most common form of fundraising: the private placement.[31] Non-accredited investors were able to participate in certain types of offerings like Regulation A and fully registered offerings, but these very expensive types of offerings were the first to dry up during the market crash.[32] In short, there was a problem with finding legal and affordable means to match the large supply of non-accredited investors with the large demand for capital by smaller issuers.

Crowdfunding also provided an option that was much needed by smaller issuers for several reasons. First, these issuers traditionally were not able to afford the costs of raising funds. For existing small businesses, even the costs of a private placement or SCOR (Small Corporate Offering Registration) offering can be substantial.[33]

Next, even if these companies could afford the costs, the success of such an offering was necessarily tied to the size of the company's network of "three Fs"—friends, family, and fools—available to the issuer.[34] Without enough people in the potential investor pool, a

-changes-to-accredited-investor-standards-18-crowdfunders-react/#5497b7fe12f2 (reporting estimations of the number of accredited investors in the country).

30. *See id.*

31. *See* John S. Lore, *The Most Common Exemption—Regulation D Rule 506*, CAP. FUND L. GROUP, http://www.capitalfundlaw.com/2015/04/05/the-most-common-exemptionregulation-d-rule-506/ (last visited Mar. 31, 2017) ("Rule 506 is the most commonly relied upon exemption in private offerings (accounting for more than 90% of offerings, according to SEC statistics).").

32. *Cf.* SCOTT BAUGESS ET AL., CAPITAL RAISING IN THE U.S.: AN ANALYSIS OF THE MARKET FOR UNREGISTERED SECURITIES OFFERINGS, 2009–2014 1 (2015), https://www.sec.gov/dera/staff-papers/white-papers/unregistered-offering10-2015.pdf ("Capital formation through private placement of securities has increased substantially since the onset of the financial crisis. Amounts raised through unregistered securities offerings have outpaced the level of capital formation through registered securities offerings during recent years, and totaled more than $2 trillion during 2014.").

33. *See, e.g.*, Mike Goodrich, *Raising Money: What Is a Private Placement Memorandum (PPM) and When Do You Need One?*, WELD: BIRMINGHAM'S NEWSPAPER (June 19, 2012), http://weldbham.com/blog/2012/06/19/raising-money-what-is-a-private-placement-memorandum-ppm-and-when-do-you-need-one/ (estimating that a quality private placement memorandum can be prepared for around $20,000).

34. *See* David T. Schneider, Can Equity Crowdfunding Crowd-Out Other Alternative Sources of Finance? 15–18 (Sept. 12, 2016) (unpublished M.S. thesis,

cash-strapped issuer will not be able to justify the costs of fundraising compliance. Even if an issuer has a built-in network of enthusiastic supporters,[35] these individuals often do not have enough money to make substantial investments in companies, at least not the kind that can truly jumpstart a business.

Finally, these smaller issuers often do not have the history of operations, if any history, necessary to attract attention from the types of institutions that offer capital in smaller amounts. Angel investors and venture capitalists also often demand an active role in the management of a company in which they invest. Conversely, owners of closely-held issuers, whose livelihoods can depend on the flexibility of company operations, may be hesitant to select any fundraising option that cedes significant control to an unknown outsider.

Although seemingly negative, the same factors listed above also provide small issuers some key benefits that they may not otherwise access. The JOBS Act offers (1) an *affordable* fundraising option that (2) reaches enough potential *investors*, (3) with enough available *capital*, (4) all *without* requiring a significant shift in *management* control.[36]

B. The "How": Use of the Internet and Portals

An important corollary to the innovative expansion of offerings to non-accredited investors was the use of the Internet in general, and social media in particular, as a medium to reach the crowd.[37] In fact, the models on which investment crowdfunding was patterned—

HEC Paris), http://www.vernimmen.net/ftp/160912_Thesis_David_Schneider_vF.pdf (providing a helpful chart breaking down types of investors and the amounts and types of projects they support).

35. *See* Stacy Cowley, *Tired of Waiting for U.S. to Act, States Pass Crowdfunding Laws and Rules*, N.Y. TIMES (June 3, 2015), http://nyti.ms/1GZIym1.

36. *See generally* Mlopes, *Why Is Crowd Funding a Good Idea?*, CROWDFUNDING AM. (Dec. 6, 2011), http://crowdfundingamerica.blogspot.com/2011/12/why-is-crowd-funding-good-idea.html (discussing benefits of crowdfunding in general).

37. *See* Peter J. Loughran et al., *The SEC Hands out a Halloween Treat to Crowdfunding Supporters*, A.B.A. BUS. L. TODAY (Dec. 2015), http://www.americanbar.org/publications/blt/2015/12/06_loughran.html ("Title III and Regulation Crowdfunding seek to model popular websites like Kickstarter and IndieGoGo, for securities offerings . . . .").

exemplified by the practices of Kickstarter[38] and Indiegogo[39]—almost certainly owe their success to the fact that projects can reach a vast network via social media platforms.[40] Campaign founders on these crowdfunding platforms prove the worth of their projects via short videos.[41] The projects are then judged by the "wisdom of the crowd"[42] at large, instead of being limited to backers in the person's[43] direct personal network. Historically, however, communication with such a large number of non-accredited strangers (for example, via a publicly available Facebook post or Tweet) would have run afoul of securities law.[44]

The fact that "[o]nline capital raising is . . . at its core a 'general solicitation'" exists in tension with the general ban on advertising and solicitation of unregistered offerings in the rest of securities

38. *See About Us*, KICKSTARTER, https://www.kickstarter.com/about (last visited Mar. 31, 2017).

39. *See How It Works*, INDIEGOGO, https://www.indiegogo.com/how-it-works (last visited Mar. 31, 2017).

40. *See* Dara Fontein, *The Secret to the Best Kickstarter Campaigns Is Social Media*, HOOTSUITE (Sept. 2, 2015), https://blog.hootsuite.com/the-best-kickstarter-campaigns-secret-weapon-is-social-media/ ("Community is the backbone of any Kickstarter project, so how you use social media can make or break a campaign.").

41. *See, e.g.*, Jessica Taige, *Jessie's Nutty Cups: Help Spread the Nutty-ness!*, INDIEGOGO, https://www.indiegogo.com/projects/jessie-s-nutty-cups-help-spread-the-nutty-ness#/ (last visited Mar. 31, 2017).

42. *See* Jamie Hopkins & Katie Hopkins, *Not All That Glitters Is Gold—Limitations of Equity Crowdfunding Regulations*, 16 DUQ. BUS. L.J. 1, 9–10 (2013) (quoting U.S. SEC. & EXCH. COMM'N, STATEMENT REGARDING THE PROPOSING RELEASE ON CROWDFUNDING (Oct. 23, 2013) (statement of Comm'r Kara M. Stein)).

43. Typically, it is individuals seeking funding that use these models, rather than companies. *See, e.g.*, Zack "Danger" Brown, *Potato Salad*, KICKSTARTER, https://www.kickstarter.com/projects/zackdangerbrown/potato-salad/description (last visited Mar. 31, 2017). *But see, e.g.*, *Oculus Rift: Step into the Game*, KICKSTARTER, https://www.kickstarter.com/projects/1523379957/oculus-rift-step-into-the-game (last visited Mar. 31, 2017) (demonstrating a notable exception to the generalization that individuals rather than companies use these models). Sometimes, it is a mix of the two—individuals trying to start their small businesses. *See, e.g.*, Taige, *supra* note 41.

44. There simply was not an exemption from registration which permitted advertising to non-accredited strangers. This is problematic because "Title III investments [are] the riskiest class—and [are] being peddled to the most unsophisticated and vulnerable class of investors." Samuel Guzik, *SEC Quietly Injects Life into Title III Crowdfunding Solicitation!*, CROWDFUND INSIDER (June 27, 2016, 7:30 AM), https://www.crowdfundinsider.com/2016/06/87260-sec-quietly-injects-life-title-iii-crowdfunding-solicitation/.

law.[45] Under Title III of the JOBS Act, however, Congress solved this problem by conscripting the web-based platforms hosting these offerings to act as "portals" in much the same way as underwriters and broker-dealers.[46] These portals act as the front-line of investor protection, serving multiple functions: gatekeepers to the official offering documents,[47] market signals of regulatory compliance for the offering,[48] and policing agents to verify individual investor qualifications and limits.[49] Once the issuer files its Form C with the SEC, it is still severely—though not entirely—restricted in the

45. Georgia Quinn, *Advertising, Social Media and the New World of Crowdfunding*, CROWDFUND INSIDER (Jan. 30, 2014, 8:00 AM), https://www.crowdfundinsider.com/2014/01/30968-advertising-social-media-new-world-crowdfunding/ (raising a potential securities law pitfall in the fact that crowdfunding online "intuitively lends itself to the use of the multitude of social media outlets"). The ban on general solicitation (absent registration) of a securities offering is longstanding and subject to only a limited number of exceptions. *See id.*

46. In fact, a registered broker-dealer can serve as the portal. *See Regulation Crowdfunding: A Small Entity Compliance Guide for Crowdfunding Intermediaries*, U.S. SEC. & EXCHANGE COMMISSION, https://www.sec.gov/divisions/marketreg/tmcompliance/cfintermediaryguide.htm (last visited Mar. 31, 2017) (identifying who can act as a crowdfunding intermediary and requirements for both intermediaries and funding portals).

47. When issuers are ready to communicate with the crowd, section 4A(b)(2) of the Securities Act prohibits advertising the terms of a crowdfunding offering, "except for notices which direct investors to the funding portal or broker." *Regulation Crowdfunding Rules*, SEEDINVEST, https://www.seedinvest.com/blog/crowdfunding/regulation-crowdfunding-rules (last visited Mar. 31, 2017). Any information relating to the offering that is posted on the intermediary's website must be filed with the SEC. *Id.*; *see* 17 C.F.R. § 227.204 (2016).

48. Crowdfunding intermediaries are responsible for having a "reasonable basis" to believe that an issuer is not conducting a fraudulent offering. *See* 17 C.F.R. § 227.301. There are some commentators, however, who argue that funding portals should be allowed a much more active role in "curating" (i.e., vetting) crowdfunding offerings. *See* Darian M. Ibrahim, *Crowdfunding Without the Crowd*, 95 N.C. L. REV. 1481, 1496 (2017) (noting that even if portals themselves are not legally able to offer subjective investment advice, expert investors could provide the kind of "merits" review that would be useful to novice investors). Industry players agree with the sentiment. *See Equity Crowdfunding Rules: The Good, the Bad and the Ugly*, SEEDINVEST, https://www.seedinvest.com/blog/jobs-act/equity-crowdfunding-rules-good-bad-ugly-part-ii (last visited Mar. 31, 2017) ("Why not allow a portal such as SeedInvest, which employs former professional investors, to filter out the noise for the benefit of its investor base? Why not allow an additional layer of fraud protection on behalf of investors?").

49. Limitations on individual investors' commitments to an issuer are a new concept to securities law. *See infra* Section II.C.

content of its outside-the-portal advertising.[50] Social media distribution can serve the function of driving potential crowd-investors to the portal via hyperlinks, though admittedly not much else under the current regulations.[51] Even considering the severe restrictions, the use of the Internet in general—and social media in particular—under Reg CF remains groundbreaking for small securities offerings involving non-accredited investors in the United States.

C. *The "How Much": Per-Offering Limits, Per-Investor Limits, and Integration*

Reg CF has a $1 million yearly limit for issuers.[52] This relatively low total, at least as compared to the JOBS Act's increase for Regulation A+,[53] is in line with the goal that this style of offering help smaller businesses and startups.[54] And, as far as securities law in general goes, a smaller limit is not unusual when non-accredited investors are involved.[55]

50. *See Advertising Your Regulation CF Offering: What Issuers Need to Know*, SEEDINVEST, https://www.seedinvest.com/blog/advertising-your-regulation-cf-offering-what-issuers-need-to-know (last visited Mar. 31, 2017) ("After you launch your offering by filing your Form C with the SEC, there are only two types of communication permitted outside the platform: [c]ommunications that don't mention the 'terms of the offering'; and [c]ommunications that just contain 'tombstone' information.").

51. *See id.*; *see also* 17 C.F.R. § 227.204 (noting the limited information in a crowdfunding issuer's "tombstone" ad).

52. 15 U.S.C. § 77d(a)(6)(A) (2012); 17 C.F.R. § 227.100(a)(1).

53. *See* 17 C.F.R. § 230.251(a) (limiting Regulation A+ offerings to $20 million (Tier I) or $50 million (Tier II), depending on factors like the type of financial audits involved).

54. *See* Press Release, U.S. Sec. & Exch. Comm'n, SEC Adopts Final Rules to Facilitate Intrastate and Regional Securities Offerings (Oct. 26, 2016), https://www.sec.gov/news/pressrelease/2016-226.html.

55. *See id.* Until recently, Rule 504 of Regulation D, which allows unlimited numbers of non-accredited investors, had an identical annual limit; the new limit is $5 million. *Id.* The increased dollar limits of revised Rule 504 may increase its desirability relative to current Reg CF. However, the Rule 504 advertising restrictions (when targeting non-accredited investors, at least) will remain a comparative detriment to Reg CF's (restricted) embrace of Internet advertising. *Compare* 17 C.F.R. § 230.504 (incorporating § 230.502's advertising restrictions), *with id.* § 227.204 (restricting issuers from advertising terms of an offer).

What *is* new to the realm of securities fundraising options is the limitation on yearly investments by a given investor.[56] Under Reg CF, not only are issuers limited in yearly fundraising, but individual investors are also capped, depending on certain income and net worth factors.[57] If either the annual income or net worth of an investor is below $100,000, the limit is calculated one way.[58] If both the annual income and net worth of an investor are $100,000 or above, the calculation is different.[59] And in no case is *any* investor, accredited or not, allowed to invest more than $100,000 in Reg CF offerings in one year.[60] The upshot here is that any Reg CF offering of $1 million will require at least ten extremely wealthy, and extremely convinced, backers to hit the yearly cap. More likely of course, and as explored in the actual data in more detail *infra*, is the situation where several hundred backers are required for a successful offering.

A positive feature of Reg CF offerings is that they are not subject to integration with other securities offerings.[61] This should mean that issuers are free to experiment with crowdfunding offerings without fear of losing the protection of other exemptions. In theory,

56. *See* Christopher Mirabile, *2016 Crowdfunding Rules: How the Restrictions Work and Why It Matters*, INC. (Apr. 11, 2016), http://www.inc.com/christopher-mirabile/2016-crowdfunding-rules-how-the-restrictions-work-and-why-it-matters.html.

57. *Id.*; *see* 17 C.F.R. § 227.100; *Regulation Crowdfunding: A Small Entity Compliance Guide for Issuers*, U.S. SEC. & EXCHANGE COMMISSION (May 13, 2016), https://www.sec.gov/info/smallbus/secg/rccomplianceguide-051316.htm (providing a handy chart illustrating how to determine one's investment limit). Although somewhat similar to the income and net worth standards which qualify an investor as "accredited" (and thus unlimited in yearly investing), the Reg CF investor limit calculations have numerically different thresholds. *See* 17 C.F.R. § 227.100; *Regulation Crowdfunding: A Small Entity Compliance Guide for Issuers*, supra.

58. *See* § 227.100(a)(2)(i) (limiting the amount to "[t]he greater of $2,000 or 5 percent of the lesser of the investor's annual income or net worth if either the investor's annual income or net worth is less than $100,000").

59. *See id.* § 227.100(a)(2)(ii) (limiting the amount to "10 percent of the lesser of the investor's annual income or net worth . . . if both the investor's annual income and net worth are equal to or more than $100,000").

60. *See id.* (limiting the amount to "10 percent of the lesser of the investor's annual income or net worth, *not to exceed an amount sold of $100,000*, if both the investor's annual income and net worth are equal to or more than $100,000" (emphasis added)).

61. *See* Regulation Crowdfunding, 80 Fed. Reg. 71,388, 71,494 (Nov. 16, 2015) ("[A]n offering made in reliance on Section 4(a)(6) is not required to be integrated with another exempt offering . . . .").

deliberate sequencing of a crowdfunding offering could also serve a vetting function for a later private placement.[62] A similar funding-begetting-funding situation may be possible if the fundraising monies are used to satisfy a lender that sufficient borrower's equity is backing an enterprise.[63] Avoiding the legal fees associated with ensuring integration compliance is yet another reason to prefer investment crowdfunding as a securities fundraising technique.

D. The "How Else": Intrastate Crowdfunding and SCOR Offerings

Of course, crowdfunding at the federal level does not exist in a vacuum. Some of the reasons why "private placement exemptions [are] generally unavailable for crowdfunding transactions, which are intended to involve a large number of investors and not be limited to investors that meet specific qualifications,"[64] have already been discussed. Issuers have several other options at the state level with which to raise funds.

As of the end of 2016, thirty-three states have intrastate crowdfunding laws on the books.[65] These laws may have significantly higher annual maximums than Reg CF.[66] But they also come with restrictions that can compare unfavorably to their federal counterpart. These intrastate crowdfunding laws roughly fall into two models.

62. This would be analogous in effect, if not cost, to the "testing the waters" stage allowed in Regulation A+ offerings. *See* Michael Raneri, *Testing the Waters and Filing a Regulation A+ Offering with the SEC*, FORBES (May 26, 2015, 5:52 PM), http://www.forbes.com/sites/mraneri/2015/05/26/testing-the-waters-and-filing-a-regulation-a-offering-with-the-sec/#435826499dec ("[T]he 'Testing the Waters' stage is relatively informal. Issuers can use public channels like social media or email to let investors know they're considering offering securities . . . .").

63. A similar technique is included in the projections used for the MNvest crowdfunding raise for Torg Brewery. *See generally* TORG BREWERY, LLC, INVESTOR PACKAGE (Dec. 16, 2016) (on file with author).

64. *See* Regulation Crowdfunding, 80 Fed. Reg. at 71,389.

65. *See* NASAA INTRASTATE OVERVIEW, *supra* note 6 (listing effective dates for thirty-two laws, with Wyoming's effective July 1, 2017).

66. *See Informed Investor Advisory: Crowdfunding*, NASAA, http://www.nasaa.org/12842/informed-investor-advisory-crowdfunding/ (last updated May 2016) ("These amounts range from $100,000 to $4 million in a 12-month period, and $100 to $100,000 per investor, unless accredited.").

The first model is based on Rule 504[67] and, depending on state law, traditionally allows an issuer to advertise the sale of registered securities to accredited and non-accredited investors.[68] But the costs associated with creation and filing of registration materials can make this type of Rule 504 usage cost-prohibitive for business startups.[69] Other options under Regulation D might allow even freer sales of securities to accredited investors only. However, accredited investors do not a "crowd" make.

The second model is based on section 3(a)(11) of the Securities Act plus SEC Rule 147[70] and/or 147A.[71] This model is by far the most common nationwide.[72] Importantly, these laws do not currently allow for general advertising or solicitation via the Internet.[73] That will soon change;[74] but even once Internet advertising becomes

67. *See, e.g.*, ME. REV. STAT. ANN. tit. 32, § 16304.6-A.D (West, Westlaw through 2015 2d Reg. Sess.) ("The offering meets the requirements of the federal exemption . . . in 17 Code of Federal Regulations, Section 230.504 (2013). . . .").

68. *See* MINN. STAT. § 80A.50(b)(2) (2016) ("The securities offered must be exempt from registration . . . pursuant to Rule 504 of Regulation D . . . ."); *see also Fast Answers: Rule 504 of Regulation D*, U.S. SEC. & EXCHANGE COMMISSION, https://www.sec.gov/answers/rule504.htm (last updated Oct. 27, 2014).

69. *See* Goodrich, *supra* note 33; *see also SCOR Forms*, NASAA, http://www.nasaa.org/industry-resources/corporation-finance/scor-overview/scor-forms/ (last visited Mar. 31, 2017) (hosting downloadable forms for the "Small Corporate Offering Registration" or "SCOR" offering, including the 118-question Form U-7).

70. *See, e.g.*, MINN. STAT. § 80A.461 (describing the MNvest statutory codification, which requires compliance with *both* section 3(a)(11) *and* Rule 147).

71. The recent creation of Rule 147A, with its exemption where intrastate crowdfunders can freely advertise and solicit on the Internet, will likely mean that many states will consider amending their statutes. *See* Final Rules 147/147A, *supra* note 9.

72. *See* NASAA INTRASTATE OVERVIEW, *supra* note 6.

73. One of the major reasons the SEC created Rule 147A as a standalone exemption was because the existing Rule 147 acts as a safe harbor to section 3(a)(11), which only works if all "offers" *and* "sales" are in-state. *See* Final Rules 147/147A, *supra* note 9. State crowdfunding laws based on the section 3(a)(11) plus Rule 147 model thus effectively barred issuers from the use of the Internet. *See* Joyce, *supra* note 9, at 357–58.

74. *See, e.g.,* Georgia Quinn, *Advertising, Social Media and the New World of Crowdfunding*, CROWDFUND INSIDER (Jan. 20, 2014, 8:00 AM), https://www.crowdfundinsider.com/2014/01/30968-advertising-social-media-new-world-crowdfunding/ ("Although [retail crowdfunding is] not legal at this time, many people are preparing for crowdfunding permitted under Title III of the JOBS Act and currently proposed Regulation CF or 'retail crowdfunding.'").

permissible, issuers without a devoted single-state following may lack sufficient numbers of investors to access any kind of useful capital.

To briefly summarize this overview, Reg CF offers a new and exciting way to raise capital for smaller issuers. A previously untapped group of investors is connected via modern technology to issuers who previously would have been unable to afford the costs of fundraising. Internet portals have been inserted as gatekeepers for investor protection and facilitation of offerings. There are also new restrictions, though. Investors and issuers are subject to relatively small investment and fundraising limits, and access to the offerings is highly structured. Intrastate alternatives provide even more options for the prospective issuer but are subject to unique statutory restrictions on advertising and solicitation. Thus, despite the numerous options for crowdfunding and crowdfunding-esqe fundraising, even the most deserving crowdfunding projects run the risk of failure if not crafted properly. Next, Part III will dissect some statistics of the first eight months of Reg CF offerings, with an eye toward recommending best practices in Part IV.

III. REGULATION CROWDFUNDING OFFERINGS BY THE NUMBERS

After a four-year-and-one-month delay during rulemaking, May 16, 2016, marked the end of a long wait for Reg CF and the beginning of a new and exciting era in peer-to-peer investing.[75] Demand had certainly pent up, as that launch date presented ten active federal funding portals with approximately thirty-two offerings.[76] Over the remainder of the year, the number of platforms would double, and the number of offerings would balloon to 186.[77]

75. *See* Regulation Crowdfunding, 80 Fed. Reg. 71,388, 71,388 (Nov. 16, 2015) ("The final rules and forms are effective May 16, 2016 . . . ."); Neiss, *supra* note 4 and accompanying text.

76. *See* JD Alois, *Week One: How Are Title III Crowdfunding Platforms Doing?*, CROWDFUND INSIDER (May 24, 2016, 10:01 AM), http://www.crowdfundinsider.com/2016/05/86040-week-one-how-are-title-iii-crowdfunding-platforms-doing.

77. The authors are grateful to Sherwood Neiss and the folks at Crowdfund Capital Advisors (CCA) for the use of their data reporting on 2016 Reg CF offerings. CCA analyzed all 186 Form C filings with the SEC in 2016 and tracked the performance of issuers throughout. A recorded webinar summary of their findings, reported in substantial portion herein, is publicly available at Sherwood Neiss & Jason Best, CCA Grp., *2016 Regulation Crowdfunding Year End Analysis*, YOUTUBE (Jan. 11, 2017), https://youtu.be/j4sQpN1cJpE [hereinafter *CCA Data*]. Discussion of the 186 offerings begins about eight minutes into the video. Citations to other

In this Part, the article dives into the data behind all 186 offerings to uncover themes and ultimately offer takeaways in Part IV.

It is worth noting at the outset that 186 offerings in an eight-month period is still a relatively small sample size upon which to make judgments. Nonetheless, it is a large enough sample size to see storyline progress. For instance, the first storyline is that of 338 offerings, 145 hit their minimum funding target.[78] This equates to a 43% success rate, a remarkably similar success rate to Kickstarter,[79] the predecessor in many ways to investment crowdfunding.

Just as in a democracy where the public elects worthy candidates by voting, in crowdfunding the crowd "elects" worthy offerings by voting with their wallets.[80] Based upon this early data, 58% of offerings are failing to meet their goal, and that is perfectly acceptable. The crowd, in its infinite wisdom, is deciding who is worthy of capital.[81]

Some commentators may seek to exploit this failures data in order to prove Reg CF's unworthiness. These commenters would be armed with the additional news that the Financial Industry

commentators' crowdfunding reports can be found at *supra* note 13.

78. *CCA Data*, *supra* note 77.

79. *See Stats*, KICKSTARTER, https://www.kickstarter.com/help/stats (last visited May 12, 2017) (reporting successful funding of 124,612 projects out of a total of 352,636 project launches, a 35.34% success rate); *CCA Regulation Crowdfunding Indices*, *supra* note 13.

80. *Cf.* John S. Wroldsen, *The Crowdfund Act's Strange Bedfellows: Democracy and Start-Up Company Investing*, 62 U. KAN. L. REV. 357, 361 (2013).

> Like successful candidates in democratic elections, crowdfunding prowess derives from large numbers of equal followers, not from small groups of influential or wealthy contributors. It is democratic insofar as any idea that captures the attention of the crowd can attract substantial amounts of money, typically in low-dollar contributions from numerous people, similar to how politicians achieve electoral success in a democracy by winning the support of many voters who each casts a single vote.

Id.

81. It should be noted that the Reg CF statistics, while premature, are in line with data from other countries, such as Australia. That is, a significant portion of all offerings are not ultimately successfully funded. *Cf.* Andy Kollmorgen, *Crowdfunding Risks, Rewards and Regulation*, CHOICE (Feb. 15, 2016), https://www.choice.com.au/money/financial-planning-and-investing/stock-market-investing/articles/crowdfunding-risks-and-rewards (comparing Australian platform Pozible's claim of 55% success to Kickstarter's 43% success in mid-2014).

Regulatory Authority (FINRA)- and SEC-registered portal, uFundingPortal, was shut down by administrative order—an Acceptance, Waiver and Consent (AWC) filed by FINRA—in November 2016 for not adhering to basic regulatory requirements.[82] Critics could characterize the fact that both of these important regulatory bodies missed uFundingPortal's malfeasance as evidence that crowdfunding is somehow inherently risky and could never adequately protect investors. Yet, wiser observers counter that this is simply a healthy system ridding itself of unfit portals and issuers.[83]

Nearly $18,000,000 in capital was invested into Reg CF issuers in the abbreviated time span of May 16, 2016, to December 31, 2016.[84] "This money was raised in a fraction of the time that it would have taken if these entrepreneurs had gone to venture capitalists. It was also raised by many companies that don't qualify for VC capital because they don't hit the sweet spot for VC investment."[85] This quote is especially powerful considering that many of the 2016 Reg CF issuers were (1) pure startup companies and/or (2) stemming from alternative industries.[86] Either of these facts can be

82. JD Alois, *FINRA Action on uFundingPortal: Potential for Fraud Found on Crowdfunding Platform*, CROWDFUND INSIDER (Dec. 13, 2016, 10:37 AM), http://www.crowdfundinsider.com/2016/12/93663-finra-action-ufundingportal-potential-fraud-found-crowdfunding-platform. Notably, uFundingPortal had listed potentially fraudulent issuers that

> had an impractible [sic] business model, oversimplified and overly-optimistic financial forecasts, and other warning signs. For example, 13 of the issuers—despite having different business models—all coincidentally listed identical amounts for their target funding requests, maximum funding requests, price per share of stock, number of shares to be sold, total number of shares, and equity valuations. None of these 13 issuers reported any assets or history of operations before May 2016, and each claimed an unrealistic, unwarrented [sic], and identical $5 million equity valuation.

Id.

83. *See* Nathaniel Popper, *Doubts Arise as Investors Flock to Crowdfunded Start-Ups*, N.Y. TIMES (Jan. 24, 2017), https://www.nytimes.com/2017/01/24/business/dealbook/crowdfunding-fraud-investing-startups.html (highlighting prominent crowdfunding consultant Sherwood Neiss, who said "that he was confident that the crowd had enough wisdom to screen out the bad companies and those that were not providing enough information").

84. *CCA Data*, *supra* note 77, at 8:13.

85. Neiss, *supra* note 4.

86. *CCA Data*, *supra* note 77.

disqualifying from a venture capital perspective, where mature companies from the technology industry fare best.[87]

Among the top six industries in 2016 Reg CF offerings, farming and fishing, wine and spirits, transportation, and food and beverage were all represented.[88] One would be hard pressed to find any data supporting strong venture capital interest in any of the aforementioned industries. Healthcare and entertainment/media were also represented; however, those industries have never shied from venture capital.[89]

What may be most astounding from the 2016 Reg CF results is the average number of investors per closed offering, which was 331.[90] Whereas a traditional "friends and family" private round conservatively may yield ten to twenty investors, we are seeing an increase on the order of more than ten times that so far in Reg CF offerings.[91] The question is whether such a large influx of investors into a young and presumably small company is feasible and sustainable in the long run. What's more, will future investors balk at such a large capitalization table? For this reason and others, some issuers, often with the help of a funding portal, create a special

87. *See* Niall McCarthy, *Which Industries Attract the Most Venture Capital?*, FORBES (June 27, 2016, 9:12 AM), http://www.forbes.com/sites/niallmccarthy/2016/06/27/which-industries-attract-the-most-venture-capital-infographic ("[S]oftware receives the largest slice of the VC pie by a considerable distance, accounting for 36.2 percent (nearly $12 billion) of all investment over the past year. Biotechnology was in second place with 17.3 percent ($5.7 billion) while media and entertainment rounded off the top three with 9.5 percent ($3.2 billion)."); Dileep Rao, *Why 99.95% of Entrepreneurs Should Stop Wasting Time Seeking Venture Capital*, FORBES (July 22, 2013, 10:00 AM), https://www.forbes.com/sites/dileeprao/2013/07/22/why-99-95-of-entrepreneurs-should-stop-wasting-time-seeking-venture-capital ("Most VCs like to invest in ventures after the potential has been proven and the risk reduced.").

88. *CCA Data*, *supra* note 77.

89. *See* PWC/CB INSIGHTS, MONEYTREE REPORT Q4 AND FULL-YEAR 2016 13 (2016), http://pwc.to/2jbyJMd.

90. *CCA Data*, *supra* note 77.

91. *Cf.* Miguel Vega, *What Is the Difference Between "Friends and Family", Seed and Series A Financings?*, COOLEY GO, https://www.cooleygo.com/difference-friends-family-seed-series-financings/ (last visited Mar. 31, 2017) (describing the differences between various start-up options).

purpose entity (SPE) in order to house investors.[92] Part IV takes a deeper look into the unique solutions and issues created by SPEs.[93]

The explanation for large numbers of average investors per closed offering is largely related to the average commitment per investor at only $833.[94] At this rate, a company would need well over a thousand investors to reach the maximum raise of $1,000,000. This dollar amount is achieved by low minimum investment amounts set by issuers.[95] Certain psychological theory contends that whichever amount is set as the minimum is what the majority of investors choose as their investment amount.[96] This phenomenon is called "anchoring," where a cognitive bias influences a person to rely too heavily on the first piece of information received.[97]

Applied to investment crowdfunding, anchoring impacts issuers in that a certain portion of investors can be expected to invest the minimum, to take a flyer on an interesting opportunity.[98] It is tough to estimate how many investors will choose the minimum, but in one recent state crowdfunded offering, 75% of the investors invested the minimum investment amount of $5000.[99] Issuers ought to be cognizant of this effect and not set the minimum too low.

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92. Amy Wam & Jillian Sidoti, *Why "Special Purpose Entities" Are So Special*, CROWDFUND INSIDER (Sept. 12, 2016, 2:49 PM), https://www.crowdfundinsider.com/2016/09/90049-special-purpose-entities-special/.

93. *See infra* Part IV.

94. *CCA Data*, *supra* note 77.

95. *See* David M. Freeman, *$100 Minimum Investment Levels Will Drive Socially Motivated Investing*, FIN. POISE (July 6, 2016), https://www.financialpoise.com/columns/crowdfunding-for-investors/100-minimum-investment-levels-will-drive-socially-motivated-investing/.

96. *See* Albert Phung, *Behavioral Finance: Key Concepts—Anchoring*, INVESTOPEDIA, http://www.investopedia.com/university/behavioral_finance/behavioral4.asp (last visited Mar. 31, 2017).

97. *See* Linda Sapadin, *The Anchoring Effect: How It Impacts Your Everyday Life*, PSYCHCENTRAL: WORLD OF PSYCHOL. (July 27, 2013), http://psychcentral.com/blog/archives/2013/07/27/the-anchoring-effect-how-it-impacts-your-everyday-life/.

98. *See The Guide to Equity Crowdfunding*, CROWDFUNDER, https://blog.crowdfunder.com/crowdfunding-startups/the-guide-to-equity-crowdfunding/ (last visited Mar. 31, 2017).

99. UNMAPPED BREWING CO., INVESTOR PACKAGE (Sept. 9, 2015) (on file with author); *see also Investing in Unmapped Brewing*, UNMAPPED BREWING, http://www.unmappedbrewing.com/#investing-unmapped-brewing (last visited Mar. 31, 2017) (indicating minimum investment of $5000). Author Zach Robins was counsel for Unmapped during this offering.

Yet, positive trends indicate that the minimum investment per Reg CF offering is increasing.[100] When Reg CF launched in May 2016, the average commitment per investor was $750.[101] Excepting a small dip shortly thereafter, the minimum commitment only continued to grow through the end of year.[102] It is expected that the average commitment will reach $1000 in 2017, which is an encouraging development from the viewpoint of investor-relations management.[103]

Company valuation is another key factor in seeking investors. This vital component of an offering sets the worth of a company and effectively determines what "piece of the pie" equity investors will be receiving in exchange for cash.[104] The data shows that despite a handful of outliers, valuations for Reg CF offerings have a median of $5,300,000,[105] which is in line with venture capital seed stage valuations at $5,900,000 (using the most recently available data).[106] This Reg CF valuation data point is especially encouraging, because in a Reg CF offering the *issuers* are able to set the valuation, whereas in a venture capital transaction the *investors* set the valuation.[107] Since Reg CF issuers now hold more leverage in setting deal terms, there was the possibility of abuse from early issuers. However, once again the data shows Reg CF valuations were not only in-line with, but actually less than, seed stage venture capital valuations.[108]

100. *CCA Data*, *supra* note 77.

101. *Id.*

102. *Id.*

103. *Id.*

104. Suspiciously high valuations are also cause for concern when an issuer's business operations cannot support them. *Cf.* Alois, *supra* note 82 (illustrating how a pattern of identical and identically-unsupported valuations—due to identical absence of operating histories—ultimately piqued regulators' suspicions at uFundingPortal).

105. This number excludes three outlier campaigns. With these campaigns included, the valuation increases to $8.9M. *See* Neiss, *supra* note 4.

106. GARRET JAMES BLACK, PITCHBOOK, 1H 2016 VC VALUATIONS REPORT 7 (2016), http://files.pitchbook.com/pdf/PitchBook_1H_2016_VC_Valuations_Report.pdf.

107. *See generally* Goncalo de Vasconcelos, *Valuations in Crowdfunding: Are We All Barking Mad?*, FORBES (May 27, 2015, 3:30 AM), https://www.forbes.com/sites/goncalodevasconcelos/2015/05/27/valuations-in-crowdfunding-are-we-all-barking-mad/#52a4dae55424 (describing the disparity in valuation between company-led crowdfunding platforms versus investor-led platforms).

108. It should be noted that "seed stage" venture capital is the category most

It is worth noting that certain industries in particular skewed the Reg CF valuations. For instance, not surprisingly, software was more than double the average valuation at $12,125,000.[109] Renewable energy offerings, perhaps due to the industry's nascence, rounded out the bottom end with $1,195,000 as the average valuation.[110] Transportation and farming and fishing sectors represented the extreme outliers at $29,975,000 and $30,652,600, respectively.[111]

Yet valuations seen in a vacuum do not tell the complete story since other variables weigh heavily on company value—namely, age and maturity. To wit, the companies most successful at raising capital under Reg CF happen to be companies that are more than six years old.[112] Specifically, companies six to seven years old had the highest average capital committed at $420,965, and companies more than ten years old ranked second at $336,175.[113] Clearly, when it comes to average capital committed, older is better. Nonetheless, the plurality of companies (39%) raising capital through Reg CF are less than one year old.[114] These same companies pulled in 43.5% of all Reg CF capital committed.[115] While the average capital committed, at $251,198 per campaign, is far less, comparatively, than the average for older companies, it is evident that Reg CF is well designed for pure startups, which is the stage at which companies are most challenged to raise capital.[116]

Another factor traditionally tied to valuation is company sales.[117] It remains to be seen how many of the Reg CF issuers had sales at the launch of their campaigns. If Regulation A+ (Title IV of the JOBS Act) is any indicator, many of these companies do not have any revenue at all at the time of offering.[118]

apropos to Reg CF offerings, yet some issuers may be better suited for Pitchbook's Series A category. *Cf.* BLACK, *supra* note 106, at 10–11.

109. *CCA Data*, *supra* note 77.

110. *Id.*

111. *Id.*

112. *Id.*

113. *Id.*

114. *Id.*

115. *Id.*

116. *Id.*

117. *See, e.g.*, *id.*

118. *Cf.* RICHARD SWART, THE EVOLUTION OF INVESTMENT CROWDFUNDING: EARLY DATA AND INSIGHTS, TITLE IV REG A+ 8 (2016), https://www.scribd.com/document/327099379/NextGenCrowdfundingRegA-WhitePaper-October62016 (finding

The average capital committed per successful campaign was $226,578, and the median minimum funding target was $50,000.[119] These successful campaigns took an average of forty-five days to hit the minimum and an average of ninety-seven days to hit the maximum.[120] For all Reg CF campaigns, the median length was 108 days, and the average length was 132 days.[121]

In the aggregate, companies younger than four years in age raised approximately 77% of Reg CF capital.[122] It will be interesting to see whether older companies (in this case companies four years and older) will comprise a larger portion of Reg CF issuers in the future. As Reg CF becomes more well known as a financing option, presumably more established companies will take advantage.

A total of 21,550 investors committed capital through all 186 Reg CF offerings.[123] Nearly 68% of the investors were represented by one single federal funding portal, Wefunder.[124] Some experts believe that more than 43,000 investors will participate in Reg CF in 2017.[125]

Reg CF issuers need to be aware of the costs of raising capital, with one of the largest costs being fees paid to the federal funding portal.[126] These platform costs were on average $11,239 per successful campaign.[127] Some portals also receive compensation in the form of warrants (in order to participate in the upside), miscellaneous fees, and expense reimbursement.[128] Wefunder and

that seventy-nine of the 131 offerings studied were by firms reporting no revenue).

119. *CCA Data*, *supra* note 77.

120. *Id.*

121. *Id.*

122. *Id.*

123. *Id.*

124. *Id.*; *cf. The Current Status of Regulation Crowdfunding*, *supra* note 12 (reporting that Wefunder offerings account for 67% of investment volume, 65% of successful offerings, and 68% of total investments, as of February 12, 2017). According to CCA, Wefunder represented 14,622 of Reg CF investors. *CCA Data*, *supra* note 77.

125. *CCA Data*, *supra* note 77.

126. *See* Louis A. Bevilacqua, *How Much Does It Cost to Raise Money Through Equity Crowdfunding?*, BEVILACQUA BLOG (Sept. 26, 2016), http://bevilacquapllc.com/much-cost-raise-money-equity-crowdfunding/ (stating that the fee paid to a portal is typically between three and six percent of the amount raised, proportionally more than other fees).

127. *Id.* For an industry-wide comparison of portal costs, see *The Current Status of Regulation Crowdfunding*, *supra* note 12.

128. *CCA Data*, *supra* note 77. Warrants give the company something similar to

Mr. Crowd have taken the low fee approach, hoping to make up for lost revenue in the future by focusing on market saturation now.[129]

Of the twenty-one federal funding portals approved by the SEC and FINRA, there has been only one failure to date: uFundingPortal (UFP LLC).[130] FINRA banned the portal in December 2016 due to its failure to properly vet issuers, who, as it turns out, were not compliant with SEC regulations.[131]

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an option, where they buy shares later but on terms defined now. Letting portals take compensation in warrants means that issuers do not have to immediately shell out some money from the Reg CF offering to pay the portals. *See* Reem Heakal, *Warrants: A High-Return Investment Tool*, INVESTOPEDIA (July 4, 2017, 12:00 PM), http://www.investopedia.com/articles/04/021704.asp.

129. *See, e.g.*, *The Current Status of Regulation Crowdfunding*, *supra* note 12.

130. *See* Alois, *supra* note 82.

131. This noncompliance seems too egregious and widespread to qualify as an innocent mistake.

> [uFundingPortal] reviewed and in some cases assisted in the preparation of required paperwork filed with the SEC by 16 different issuers that offered securities through UFP's platform. UFP knew that none of the 16 issuers had filed the following required disclosures with the SEC:
>
> (1) a description of the business of the issuer, and the anticipated business plan of the issuer;
>
> (2) a description of the purpose and intended use of the offering proceeds;
>
> (3) a description of the ownership and capital structure of the issuer;
>
> (4) a discussion of the issuer's financial condition;
>
> (5) all positions and offices with the issuer held by the directors and officers (and any persons occupying a similar status or performing a similar function). The [sic] period of time in which such persons served in the position or office and their business experience during the past three years;
>
> (6) a description of how the exercise of rights held by the principal shareholders of the issuer could affect the purchasers of the securities being offered;
>
> (7) the risks to purchasers of the securities relating to minority ownership in the issuer and the risks associated with corporate actions including additional issuances of securities, issuer repurchases of securities, a sale of the issuer or of assets of the issuer or transactions with related parties;
>
> (8) a description of the restrictions on transfer of the securities;
>
> (9) a discussion of the material factors that make an investment in the issuer speculative or risky; and
>
> (10) a description of the process to complete the transaction or

In the aggregate, the funding portals are averaging four new campaigns per week.[132] Wefunder was the most prevalent portal out of the gate, launching the most offerings on day one, and continued the trend through year end, representing 29% of all campaigns.[133]

IV. RECOMMENDATIONS AND BEST PRACTICES FOR CROWDFUNDING OFFERINGS

Although Reg CF is in its infancy and funding models are still being tweaked and tested, there are nonetheless many lessons to be learned.[134] Ideally, prospective issuers and portal operators can benefit from such best practices and continue to refine their methods, meanwhile providing feedback to the investment crowdfunding community. It is going to "take a village" in order to bring Reg CF and other forms of investment crowdfunding to the forefront and consciousness of average citizens. By collaborating and sharing best practices, hopefully the rising tide will lift all boats.

By and large, the most important advice to any company contemplating investment crowdfunding is the most traditional, yet obvious advice: ensure the business plan is well thought out and thorough, as investors will quickly see through gaping holes or inexact assumptions. Certainly the ultimate success of the crowdfunded business may depend largely on the collective experience of the founders.[135] However, thoughtful planning and a

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cancel an investment commitment.

Financial Industry Regulatory Authority Letter of Acceptance, Waiver and Consent (No. 2016051563901) from Gary Shao, Managing Dir. of uFundingPortal, to Dept. of Enforcement, FINRA (Nov. 25, 2016), http://www.finra.org/sites/default/files/fda_documents/2016051563901_FDA_JG411996.pdf.

132. *CCA Data*, *supra* note 77.

133. *See id.*; *cf. The Current Status of Regulation Crowdfunding*, *supra* note 12 (reporting that Wefunder has hosted ninety-nine campaigns as of May 15, 2017).

134. The authors were unable to find other examples like this data-driven analysis in academic literature. This is probably unsurprising, given the limited time frame and limited number of offerings to date. The authors hope that this article is the first of many to periodically review and reassess the efficiency of crowdfunding models.

135. *See, e.g.*, Nathan Pierce, *MicroBrewr 066: How to Get an SBA Loan for a Startup Brewery*, MICROBREWR (May 26, 2015), http://microbrewr.com/how-to-get-sba-loan-for-startup-brewery/ ("[T]he ideal candidate should have experience working in a commercial brewery . . . . If you're a homebrewer wanting to get an SBA loan, it could help to have awards for your beer.").

well-rounded team can often make up for inexperience and pay dividends in the end. Fortunately, Reg CF requires disclosures including a "description of the issuer's business [plan]" to protect investors.[136] Rather than seeing such disclosures as a burdensome obligation, issuers ought to embrace the challenge and see this is an opportunity design a strong and viable business plan.

The SEC also mandates that issuers provide "a reasonably detailed description of the purpose of the offering, such that investors . . . understand how the offering proceeds will be used."[137] Here, the early insight shows how critical a low and achievable minimum funding target is to success. As evidenced by Reg CF data to date, if the issuer struggles to raise its minimum amount within forty-five days, the likelihood of ultimately closing on funding is diminished.[138] Once again, this advice is obvious, but some may struggle to apply it to their offering. The clear solution is to provide investors with three scenarios: worst case, average case, and best case. This three-tiered structure grants issuers the flexibility to execute on effectively different roll-outs of the business plan, contingent on how much capital is raised. For instance, an issuer could (1) in the worst case, lease premises and equipment; (2) in the average case, lease premises but purchase equipment; or (3) in the best case, purchase both premises and equipment. Even though company founders may prefer to purchase both premises and equipment, they would be better served by at least considering a worst case scenario, because they will sooner find themselves on the road to a successful offering.

With respect to minimum investments per investor, our advice is somewhat counter to the previous paragraph, in that a minimum too *low* may backfire on the company. This strategy once again relates to the psychological theory of anchoring, wherein an investor who, for example, otherwise may invest \$2000 in a company instead settles for the bare minimum \$1000.[139] Under this scenario, the issuer has lost half of the potential investment and will require twice

136. 17 C.F.R. § 227.201(d) (2016); Regulation Crowdfunding, 80 Fed. Reg. 71,388, 71,390 (Nov. 16, 2015).

137. Regulation Crowdfunding, 80 Fed. Reg. at 71,401 (Part II.B.1(a)(1)(c)(iii)).

138. *CCA Data*, *supra* note 77. One hundred thirty-two days is the average length of all Reg CF campaigns. *Id.* One hundred eight days is median length of Reg CF campaigns to date. *Id.*

139. *See supra* notes 96–98 and accompanying text.

the number of potential investors.[140] Now, it is also admittedly true that the higher the minimum investment per investor, the smaller the actual pool of willing and able investors. This is a fine line to walk, but as in any securities offering it is the company's role to figure out the "sweet spot": where enough investors are able to participate, yet the investment level is not too low.

Our advice is not to dip below $1000 per investor in an equity offering and to preferably hover between $2500 and $5000, if possible. For most offerings, this strategy will yield a capitalization table of one hundred investors or less,[141] which we believe is manageable. Once a founder, especially an unseasoned one, is left to manage investors in the triple digits, the founder may find his or her time and resources are too often being spent managing investor questions, expectations, and administrative tasks, such as transfers of interest. Additionally, issuers who are able to inform the crowd that only one hundred investors at the very maximum will be permitted to invest may benefit from the competition created to fill those spots. And, in the event one or more investors purchase a large amount of shares, the number of investors permitted could radically drop.[142] Absent a reasonably high minimum and cap on total number of investors, issuers may find themselves with close to one thousand investors,[143] an untenable situation for some.

A strategy often suggested to curb the issues arising from the sheer number of non-accredited investors on the company's cap table is to create a special purpose entity (SPE).[144] The main

140. As mentioned briefly in Section II.A, *supra*, the size of the issuer's network can play a major role in the ultimate success of a crowdfunding offering.

141. This estimate is the result of a comparison of the average committed and successful capital numbers from the text accompanying *supra* notes 116 and 119 (approximately $251,000 and $226,000, respectively) and dividing by $2500.

142. *See* 17 C.F.R. § 227.100(a)(2)(ii) (2016) (allowing an annual investment of up to $100,000 for the wealthiest investors).

143. *E.g.*, *Cleveland Whiskey*, WEFUNDER, https://wefunder.com/cleveland.whiskey (last visited Mar. 31, 2017) (displaying a successful offering that raised $711,787 from 952 investors).

144. Note that SPEs are prohibited under the Final Rules for Reg CF, but proposed legislation, the Crowdfunding Enhancement Act, S. 1031, 115th Cong. (2017), includes a reversal of this ban; this bill was previously proposed as the Fix Crowdfunding Act in 2016 but did not make it out of the Senate, despite being passed by the House. *See* Anthony Zeoli, *The Fix Crowdfunding Act. What It Fixes & What It Does Not*, CROWDFUND INSIDER (July 28, 2016, 5:45 PM), https://www.crowdfundinsider.com/2016/07/88536-fix-crowdfunding-act-fixes-not/.

objectives to this structure are to (1) only show one investor on the issuer's capitalization table; (2) effectively silence the investors from a corporate governance standpoint; and (3) prevent a secondary market from forming where investors are trading company shares.[145] This strategy has mixed consequences in the crowdfunding context.[146] On one hand, SPEs are a strategy worth considering from the issuer's perspective, because management of the company will potentially run more smoothly and future (more sophisticated) investors may appreciate the smaller capitalization table. On the other hand, however, crowdfunded investors may get wise to some of the inherent concerns related to SPEs, such as (1) Who is creating the SPE?; (2) Who is managing the SPE?; (3) Who is covering the costs related to the SPE?; and (4) How should transfers of interests in the SPE be dealt with? On this last question, the most pressing concern is that investing in a private company is an inherently illiquid proposition. So, offering investment in an illiquid entity that itself owns interests in an illiquid entity seems to do a disservice to unsophisticated investors. Having said all of this, there are examples where SPEs are apparently working.[147]

Shifting to another truism of investment crowdfunding, we now discuss the adage that an issuer should raise as much as it can—typically in the form of verbal commitments—before commencement of the offering.[148] Anecdotally, this often shakes out to 30–40% of capital committed prior to the launch of the campaign. As a verbal commitment of course, investors are not obligated to

145. *Id.*

146. *See id.*

147. For example,

> PeerRealty invests as a single limited member into a sponsor's Limited Liability Company ("LLC") or Limited Partnership ("LP"). All PeerRealty investors are pooled into a special purpose [entity], typically an LLC, and then PeerRealty subscribes to the sponsor's entity as a single investor. This means the sponsor is only responsible for one report, one distribution and one K-1. PeerRealty processes all of the underlying reports, distributions and K-1s for our investors.

Education: Sponsor Questions, PEERREALTY, https://peerrealty.com/pages/education (click "How are investments structured?" under "Sponsor Questions") (last visited Mar. 31, 2017).

148. Of course, issuers may not officially solicit for investments until the Form C offering statement has been filed with the SEC. *See* Regulation Crowdfunding, 80 Fed. Reg. 71,388, 71,423 (Nov. 16, 2015).

follow through on their promise.[149] Nonetheless, assuming a large portion of the commitments does indeed invest, the issuer can ride that wave of investors towards a successful closing. This concept is best known as the bandwagon effect, where someone is more likely to perform an action if others have, too.[150] In more modern times, this has also been termed "FOMO," or the "fear of missing out."[151] Applied to crowdfunding, if individuals see across their social networks that friends and acquaintances support a campaign, they are more likely to follow suit.

A similar strategy to pre-funding a campaign with verbal commitments is funding via a convertible note bridge financing.[152] The capital raised here funds company operations and campaign-related expenses[153] during the campaign. In a common scenario, the issuer offers "friends and family" superior investment terms to the crowdfunded offering round.[154] These investors are rewarded for backing the company at a somewhat riskier stage by receiving a conversion discount on the back end.[155]

149. *See The Guide to Equity Crowdfunding*, *supra* note 98 (discussing the art of closing a deal with an investor).

150. *See Bandwagon Effect*, INVESTOPEDIA, http://www.investopedia.com/terms/b/bandwagon-effect.asp (last visited Mar. 31, 2017).

151. *See FOMO*, MERRIAM-WEBSTER, https://www.merriam-webster.com/dictionary/FOMO (last visited Mar. 31, 2017).

152. Convertible notes are debt instruments paying interest with a firm maturity but with the unique quality of converting into equity securities of the issuer upon a certain "trigger" such as a sales benchmark or Series A Financing. *Compare* Gordon Daugherty, *Using Verbal Commitments to Secure Your First Investors*, SHOCKWAVEINNOVATIONS (Dec. 27, 2016), https://shockwaveinnovations.com/2016/12/27/using-verbal-commits-to-secure-your-first-investors/ (explaining the use of verbal commitments to secure investments), *with* Antone Johnson, *Convertible Note Financing 101 for Startups*, BOTTOM LINE L. GROUP: MASHTAG BLAWG (Oct. 31, 2011), http://www.bottomlinelawgroup.com/2011/10/31/convertible-note-financing/ (discussing convertible note financing).

153. These campaign-related expenses can include, for example, legal, accounting, marketing, public relations, and portal fees.

154. *See, e.g.*, *How to Set Conversion Discounts in Convertible Notes*, STARTUP LAW. (Dec. 18, 2009), http://www.startuplawyer.com/seed-rounds/how-to-set-conversion-discounts-in-convertible-notes. A common example is a conversion "discount" of somewhere between ten and twenty-five percent. Effectively, upon closing of an equity crowdfunded investment round, the convertible note investors can buy shares or units at $0.80 or $0.90 on the dollar.

155. *See, e.g.*, Johnson, *supra* note 152 (discussing conversion discounts).

One of the paramount considerations for issuers is the legal structure of their company. Issuers typically choose between limited liability companies (LLCs) and C Corporations (C-Corps) as the two most common entity types.[156] However, more and more "public benefit corporations" (B-Corps) or some variant thereof are being used as a means to provide some social good in addition to profits.[157] C-Corps, despite double taxation, are the most used entities for raising capital, with 73% of all Reg CF offerings, according to CCA.[158] Further, of security types, common stock is the most widely used, representing over 47% of all C-Corp offerings.[159] Additionally, common stock offerings represent the most capital closed upon through Reg CF offerings to date, accounting for over $3.6 million.[160] Meanwhile, for LLCs, common membership units as a security type raised the most capital under Reg CF, accounting for 22%.[161] The lesson to be learned here is that simple financing structures—like corporations raising capital via common stock—offer the best opportunities to raise capital in the short term.[162]

156. *CCA Data*, *supra* note 77.

157. *Id.* At a higher level of abstraction, apparently even crowdfunding platforms themselves are reincorporating as B-Corps. *See* JD Alois, *Saving the American Dream: Wefunder Becomes a Public Benefit Corporation*, CROWDFUND INSIDER (Nov. 2, 2016, 8:10 AM), https://www.crowdfundinsider.com/2016/11/91963-saving-american-dream-wefunder-becomes-public-benefit-corporation/; Alison Griswold, *Kickstarter Wants to Be Sure You Know How Much Good It's Doing*, SLATE: MONEY BOX (Sept. 21, 2015, 4:58 PM), http://www.slate.com/blogs/moneybox/2015/09/21/kickstarter_incorporates_as_a_public_benefit_corporation_that_supports_creative.html.

158. *CCA Data*, *supra* note 77.

159. *Id.*

160. *Id.*

161. *Id.* ($1.73M out of $7.7M).

162. Over time, the crowd may become more sophisticated and open to alternative security types such as SAFEs and more complicated debt securities. SAFEs were designed by incubators in Silicon Valley. *See Startup Documents*, Y COMBINATOR (Feb. 2016), https://www.ycombinator.com/documents/. They represent a significant portion of total crowdfunding offerings, both for corporations and LLCs. *See CCA Data*, *supra* note 77. However, commentators have mixed reactions as to whether SAFEs are appropriate for unsophisticated investors. *Compare* Joseph M. Green & John F. Coyle, *Crowdfunding and the Not-So-Safe SAFE*, 102 VA. L. REV. ONLINE 168 (2016), *with* Amy Wan, *When You Use a Bomb to Swat a Fly: A Response to the Proposal of Banning SAFEs in Crowdfunding*, CROWDFUND INSIDER (Sept. 27, 2016, 12:01 PM), https://www.crowdfundinsider.com/2016/09/90501-use-bomb-swat-fly-response-proposal-banning-safes-crowdfunding/, *and* Joe Green

In addition to focusing on traditional security and entity types, issuers would be wise to incorporate investor perks into their campaigns, such as access to special company products and services. Melding Kickstarter-like rewards into investment crowdfunding campaigns can yield increased enthusiasm from investors.[163] Examples include free growlers from breweries[164] and promotional discounts on certain products.[165]

Campaigns will also see more success from strong video presentations accompanying their offering documents, once again according to CCA data.[166] Early evidence shows that campaigns with no video or a video with poor production quality fared worse in terms of raising capital.[167] CCA's analysis of the videos, although purely subjective, determined that campaigns with videos scoring an eight or higher on a scale of ten were most likely to reach the minimum funding target.[168] So, the takeaway for issuers is to invest marketing dollars into videos in order to create an emotional connection with the audience.[169]

Social network reach has been shown to be a critical component to campaign success.[170] Data aggregated from CCA cross-referenced

& John Coyle, *When It Comes to Retail Crowdfunding, SAFEty First*, CROWDFUND INSIDER (Oct. 26, 2016, 8:00 AM), https://www.crowdfundinsider.com/2016/10/91609-when-it-comes-to-retail-crowdfunding-safety-first/.

163. In fact, there are those who argue that rewards in some sense are essential to *any* crowdfunding raise. *See* Kathleen Minogue, *What Rewards Can Teach Equity Crowdfunding*, CROWDFUND BETTER (July 25, 2016), http://crowdfundbetter.com/rewards-can-teach-equity-crowdfunding/ (arguing that rewards are a way to build essential "social proof" of concept).

164. *See, e.g.*, *Invest in Hawaii Cider Company*, WEFUNDER, https://wefunder.com/hawaiicider (last visited Mar. 31, 2017) (giving free growlers to individuals investing $1000 or more in the company).

165. *See, e.g.*, *Invest in My Trail*, WEFUNDER, https://wefunder.com/mytrail (last visited Mar. 31, 2017) (offering lifetime 20% discounts to investors of $1000 or more).

166. *CCA Data*, *supra* note 77.

167. *Id.*

168. *Id.* In fact, campaigns that had any video outperformed campaigns with no video by a factor of almost 11:1. *See id.* (reporting videoless campaigns at $1,497,218 and campaigns with video at $16,447,251).

169. In many ways, this emotional connection is tied in with the concept of "social proof." *See* Minogue, *supra* note 163.

170. This is not unique to equity crowdfunding. Rewards crowdfunding campaigns also depend on extensive social network reach. *See 18 Factors that Impact How Much You'll Raise Through Crowdfunding*, USEED, https://useed.org/18-factors

against Reg CF campaigns indicates that it takes approximately 3225 connections across company founders' social networks in order to raise $50,000.[171] Extrapolated further, it takes 9275 connections to raise $250,000 and over 16,000 connections to raise $750,000.[172] Although there are certainly exceptions to this rule, it is very clear that the wider the reach a company has in social networks—whether it be Facebook, Twitter, LinkedIn, or the next hot platform—the higher the likelihood of raising capital.

Another obvious statement, though worth noting, is that issuers should avoid both launching campaigns and spending advertising dollars on the weekends and right before holidays, as both timeframes equate to low investor engagement, according to CCA.[173] Conversely, data shows that launching and/or marketing in the middle of the week leads to the highest level of investor engagement.[174]

Similar to reward-based crowdfunding campaigns on Kickstarter and IndieGoGo, constant and timely communication with investors is key.[175] According to CCA, "companies that communicated with their investors saw higher valuations than those companies that did not communicate."[176] The lesson learned is that providing progress updates engages investors, builds trust, and leads to more capital invested.

In conclusion, there is no one package, plan, or product that will guarantee issuers success. Rather, there are suggested best practices to follow both before and during offerings to increase the likelihood of reaching minimum funding. Such practices include, but are not limited to (1) simple, easy to digest securities such as common stock; (2) traditional entity structure in the form of a corporation; (3) large social networks for the directors and officers to tap into; (4) strong video production; and perhaps most importantly, (5) gaining pre-commitments from family and friends prior to launch.[177] We acknowledge that these conclusions may be

-impact-much-youll-raise-crowdfunding/ (last visited Mar. 31, 2017).

171. *CCA Data*, *supra* note 77.
172. *See id.*
173. *Id.*
174. *Id.*
175. *Id.*
176. *Id.*
177. *Id.* Preferably the pre-commitments are accomplished by a non-integrated

somewhat premature in this very nascent industry. All the same, we hope that these recommendations might provide issuers and their counsel with useful starting points when considering how to use investment crowdfunding.

V. CONCLUDING REMARKS: THE FUTURE OF CROWDFUNDING

In conclusion, investment crowdfunding offers an exciting opportunity for small issuers to access a previously untapped (and arguably untappable) pool of capital. Based on the first eight months of offerings, it is possible to draw some tentative conclusions; as each Part above includes a brief summary, they need not be repeated here. Investment crowdfunding is also an area ripe for immediate and ongoing research to see how businesses perform after the capital raise, especially as more offerings close (or fail to close) on funds.

In the meantime, it is incumbent upon lawmakers to pass legislation improving upon and easing the capital-raising process. Namely, the Crowdfunding Enhancement Act attempts to fix, among other issues, the SPE prohibition discussed above.[178] Additionally, the Crowdfunding Enhancement Act has contemplated increasing the $1,000,000 Reg CF funding limit.[179] We think these are sensible proposals for immediate action.

At the state level, amendments to many of the thirty-plus intrastate investment crowdfunding offerings are currently

convertible note offering.

178. *See* Crowdfunding Enhancement Act, S. 1031, 115th Cong. (2017), https://www.congress.gov/bill/115th-congress/senate-bill/1031.

179. *See id.* § 2. Throughout Europe, where investment crowdfunding has matured over the past decade, maximums up to $5 million are standard. JEFF LYNN & BEN THORN, CROWDFUNDING LEGISLATION REFORM: WHAT IS NEEDED AND WHY 2 (2016) (on file with author).

> If the burdens placed on issuers make raising capital through investment crowdfunding significantly more expensive, time-consuming or otherwise difficult than raising money through other channels (such as institutional or private angel investors), the consequence is not just higher costs to the issuers. Instead, it will cause businesses only to turn to crowdfunding as a last resort after more efficient capital-raising methods have failed. The result will be that ordinary retail investors will have access only to those businesses that cannot raise capital elsewhere and that, by implication, have the least chance of success.

Id. at 1.

underway[180] in order to (1) accommodate the new Rule 147A and (2) benefit from Rule 504's higher ceiling of $5,000,000.

We are also encouraged by the prospects of a new SEC chair intent on decreasing regulation in this space.[181] With the current President's wealth of business experience,[182] together with the Republican-majority Congress that generally supports his platform of business de-regulations,[183] perhaps we are embarking on a golden era of private capital funding.

However, if we are to raise over $100,000,000 in Reg CF capital as some have suggested,[184] a lack of public awareness would still hold us back. Making the public more cognizant of this new avenue to raise capital will take time, creative marketing campaigns, and perhaps the good luck of a Reg CF issuer taking a meteoric rise. The next chapter in the story of crowdfunding should be titled: Onward!

VI. POSTSCRIPT: BEST PRACTICES FOR INVESTING IN THE NEXT GENERATION OF BUSINESS LAWYERS

Editor's Note: After writing this article and as the authors prepared to participate in the symposium associated with this issue of the Mitchell Hamline Law Review*, "Lawyers as Business Leaders: The Unique Skills, Knowledge, and Perspective of a Legal Education," the authors compiled the following reflections on the symposium topic.*

A symposium on how well law schools prepare the next generation of business lawyers is either extremely timely or long

180. *See, e.g.*, H.F. No. 444, 90th Leg., 1st Sess. (Minn. 2017), https://www.revisor.mn.gov/bills/bill.php?b=House&f=HF0444&ssn=0&y=2017 (proposed 2017 MNvest amendment).

181. *See* Connie Loizos, *Why Silicon Valley Is High-Fiving over Trump's SEC Pick*, TECH CRUNCH (Jan. 26, 2017), https://techcrunch.com/2017/01/26/why-silicon-valley-is-high-fiving-over-trumps-sec-pick/ (predicting that under nominee Walter "Jay" Clayton's leadership, "the pace of deal-making will accelerate . . . including on crowdfunding platforms").

182. *See* Brody Mullins & John D. McKinnon, *In Donald Trump's Washington, Business Lobbyists Champ at the Bit*, WALL ST. J. (Jan. 10, 2017), https://www.wsj.com/articles/trump-win-puts-range-of-business-interests-back-in-play-1484044223 (discussing the current climate of excitement among U.S. businesses in anticipation of Trump's business-friendly policy).

183. Diane Stafford & Mark Davis, *Obamacare, Numerous Regulations Face Trump Reversals*, KAN. CITY STAR (Nov. 9, 2016, 5:50 PM), http://www.kansascity.com/news/business/article113776653.html.

184. *CCA Data*, *supra* note 77.

overdue, depending on who you ask. In some ways, a dialogue of how best to introduce young people into the ranks of our esteemed profession will always be relevant regardless of the particular focus, and it is our pleasure to contribute here. But in recent years, it has become patently clear that the role of lawyers, in business particularly, is changing. In general, it can no longer be assumed that the only pinnacle of law school success is a big firm job in private practice.

More and more lawyers are asked to step into leadership positions in-house, and that has brought with it heavier ethical responsibilities and higher expectations that lawyers speak the language of business. Technological breakthroughs have begun to replace some of the functions traditionally filled by junior attorneys. Today's business-focused law school graduate will be expected to speak fluently not only in legal issue-spotting, but also in balance sheets, corporate strategy, and industry politics.

To their credit, many law schools are already adjusting course to adapt to this new reality. We offer some thoughts below about the best of these trends and some suggestions as to where there might be room for improvement. These thoughts, of course, are influenced by personal experience and should therefore be received with deserved grains of salt. Feel free to disagree or demand more explanation as you wish.

Zach Robins: These days, I interact with law school via the summer associates at the law firm where I practice. For some, it is clear that they have specifically tailored their law school experience to overlap substantially with what might traditionally be considered business school subjects. Others seem entirely baffled by balance sheets and governance concepts, and this confuses me. Even if not working on corporate or transactional projects, most lawyers interact with business clients at least at some point in their career. Even non-business-focused lawyers deal with these concepts personally at some point when in a firm or government setting. Having a working knowledge of these daily concerns seems like a no-brainer. I think law schools could do a better job exposing students to these concepts earlier on.

It is not clear to me who can best "teach" this concept, but I think law students should be empowered to define their own career path. In this regard, I think law firms and other legal employers have a part to play. For example, my participation in getting the

Minnesota intrastate crowdfunding statute drafted was not due to some work assignment bestowed from on high. We had the enthusiasm, we defended the value proposition to my employer, and my firm was entirely supportive. To tie in with my earlier point, my experience with defending a business idea came in handy when advocating for a potentially negative-return time commitment. Crowdfunding issuers continue to contact the firm for assistance with their offerings, rewarding the bravery.

Tim Joyce: I was fortunate (in my opinion) to come to law school after approximately a decade in the "real world." Now, I am about to go back into the real world, one degree richer and several thousand dollars further in debt. This has caused me to think critically and objectively at many points about the value of a law degree in 2017.

From an older student's perspective, I think the most valuable thing law schools have begun to do is focus on practical and clinical experiential learning. In addition to knowledge of the law, this style of instruction (done properly—that is, graded holistically) most closely simulates the real-life experience of attorneys. For instance, my 1L class was given the opportunity to evaluate the merits of a hypothetical employment case and draft memos to both the client and the assigning partner. The assignment gave us the opportunity to practice some non-legal writing skills—formatting, tone, addressing a non-lawyer audience—that can have as much, if not more, impact on the outcome of a negotiation as the merits. In another class, we spent the semester negotiating the terms of a hypothetical LLC operating agreement while simultaneously learning the law of partnerships, LLCs, LLPs, and other business organizations. I can honestly say that concepts related to this assignment have come up literally dozens of times in my clerkship. Law schools need more classes like this one, and such classes should be more often included in graduation requirements.

In a similar vein, and I openly admit the apparent dissonance between my statements and the publication medium, I think law schools spend too much time emphasizing the benefits of participation on law reviews and journals. That is not to say that I think journals are wholly without value—I wouldn't manage the tech journal at my school if I thought that. I only think the historical prestige associated with being an editor or staffer is either no longer relevant or never was. Being an editor or staffer is fine for students interested in becoming subject-matter experts (say, in investment crowdfunding) or impressing a judge with demonstrated attention to detail. For everyone else, see my earlier comments about the value of experiential learning opportunities.