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**DON'T LET THEM FOOL YA: EXAMINING THE SEC RULES ON CROWDFUNDING
AND THEIR EFFECT ON SMALL BUSINESS GROWTH**
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Introduction

Over the past decade Crowdfunding¹ has become increasingly popular within the U.S. Crowdfunding originally was used as a way for performing artists to raise funds for their projects. Most recently, it has been used to fund projects outside of the entertainment industry. Businesses and local governments have been using this method to raise capital. Crowdfunding websites such as Indiegogo, Kickstarter, and Crowdfunder have made it easier for individuals, particularly entrepreneurs, to access capital.²

With the increase in popularity of Crowdfunding comes the need for regulation. In 2012, Congress, with bipartisan support, passed the Jumpstart Our Business Startups (“JOBS”) Act. The JOBS Act gave legitimacy to Crowdfunding as a way of raising capital. Recognizing that access to

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¹ Crowdfunding is defined as “the practice of soliciting financial contributions from a large number of people especially from the online community.” Definition of Crowdfunding, MERRIAM-WEBSTER, <http://www.merriam-webster.com/dictionary/crowdfunding> (last visited Sept. 21, 2016).

² See *About Us*, KICKSTARTER, <https://www.kickstarter.com/about?ref=nav> (last visited Aug. 22, 2016) (explaining how Kickstarter primarily helps individuals in the entertainment industry raise funds to support their projects).

capital for entrepreneurs was limited; Congress passed the bill with the hope that it would help create jobs.

The JOBS Act amended the Securities Act of 1933, and mandated that the Securities and Exchange Commission (“SEC”) promulgate rules that govern the eligibility and use of Crowdfunding.³ The SEC in 2011 and 2012 released proposed rules that would govern the Crowdfunding exemption, which eases regulation for small businesses.⁴ Critics have said that the JOBS Act and the SEC rules are both too liberal and too restrictive.

This note will discuss the SEC rules that are set to go into effect in May of 2016, and their potential effects on small business growth and investor protection. In particular, this note will highlight the potential conflict that will arise between the goal of the JOBS Act and the implementation of the SEC rules governing crowdfunding. This article will suggest that the SEC rules will only hinder the growth of small businesses instead of helping them raise capital.

Part I of this note will discuss the Securities Act of 1933 and the current regulatory scheme. Part II will discuss the JOBS Act, the background of crowdfunding, and the new SEC Rules for crowdfunding. Part III of this note will discuss the criticism of the JOBS Act and the SEC Rules. Finally, Part IV will suggest two approaches that are aimed at protecting investors while easing the requirements for small businesses thus allowing them to raise capital more easily.

Part I—The Securities Act and JOBS Act.

A. The Securities Act of 1933

³ Jumpstart Our Business Startups (JOBS) Act Pub. L. No. 112-106, [126 Stat. 306 \(2012\)](#) (codified at [15 U.S.C. §§ 77-78 \(2012\)](#)); SEC Proposed Crowdfunding Regulation, Securities Act Release No. 9470, Exchange Act Release No. 70741, 78 Fed. Reg. 66428 (proposed Nov. 5, 2013) (to be codified at 17 C.F.R. pt. 200, 227, 232, 239, 240, 249).

⁴ *See id.* The SEC later adopted the majority of the rules proposed with some revisions and amendments.

The purpose of the Securities Act of 1933 (“Securities Act”) was to prevent fraud in the sales of securities by requiring “full and fair disclosure” of the character of securities sold in the U.S. and abroad.⁵ The Securities Act was enacted after the 1929 stock market crash.⁶ Evidence showed that fraud and insider dealings resulted in the financial collapse.⁷ Prior to the passing of the Securities Act many States had their own Blue Sky Laws,⁸ but were unable to effectively enforce these laws with respect to the sale of interstate securities.⁹

The Securities Act established the Securities and Exchange Commission,¹⁰ which regulates the sale of securities in the secondary market.¹¹ Security is defined as: “any note, stock, treasury stock, security future, security-based swap, bond, debenture, evidence of indebtedness, certificate of interest or participation in any profit-sharing agreement....”¹²

Section 5 of the Securities Act controls offerings and requires that an issuer file a registration statement with the SEC before selling any security.¹³ An issuer in its registration statement must disclose information about the company and its executives.¹⁴ This allows the SEC to discover any potential fraud, and it allows investors to make informed decisions about their investment.¹⁵

Registration can cost too much money for a small business.¹⁶ Often the cost of registration exceeds the amount a business is seeking to raise. Registration costs can exceed \$100,000.¹⁷ In addition

⁵ Securities Act of 1933, Pub. L. No. 22-48, 48 Stat. 73-4 (2012).

⁶ Stuart R. Cohn & Gregory C. Yadley, *Capital Offense: The SEC's Continuing Failure to Address Small Business Financing Concerns*, 4 N.Y.U. J. L. & BUS. 1, 15 (2007).

⁷ *Id.*; see also H.R. REP. NO. 73-85, 1 (1933).

⁸ Jonathan R. Macey & Geoffrey P. Miller, *Origin of the Blue Sky Laws*, 70 TEX. L. REV. 347, 352 (1991).

⁹ Cohn & Yadley, *supra* note 5, at 15-16.

¹⁰ See *id.* at 16 (noting the Securities Act of 1934 established the SEC).

¹¹ Securities Act of 1933, 15 U.S.C. §§ 77(a)-(aa) (2012).

¹² *Id.* § 77(b).

¹³ *Id.* § 77(e).

¹⁴ Benjamin P. Siegel, *Title III of the JOBS Act: Using Unsophisticated Wealth to Crowdfund Small Business Capital of Fraudsters' Bank Accounts?*, 41 HOFSTRA L. REV. 777, 783 (2013).

¹⁵ *Id.*; see also § 77(aa).

¹⁶ See Siegel, *supra* note 13, at 788-789; see also § 77(aa).

¹⁷ C. Steven Bradford, *Crowdfunding and The Federal Securities Laws*, 2012 COLUM. BUS. L. REV. 1, 119 n.607 (2012).

to the costs, registration can be time consuming with the average time between filing and the effectiveness of an offering at roughly 103 days.¹⁸ These types of requirements make it difficult for small businesses to raise small amounts of money.¹⁹ Critics of this regulatory scheme have recognized that following such a path was not feasible for small businesses.²⁰

There are however, certain exemptions under the Securities Act that would allow an issuer to circumvent the registration process.²¹ Rules 504, 505, and 506 of Regulation D contain the main exemptions that the Securities Act allows.²² Regulation D, which was adopted in 1982,²³ allowed issuers to circumvent the registration requirements and eased the amount of disclosure required to raise capital.²⁴

Regulation A

Regulation A was a collection of rules that were issued by the SEC.²⁵ It functions as an exemption from registration for public offerings.²⁶ Regulation A, which was intended for small businesses, limited the requirements for disclosures for companies offering and selling securities to the public.²⁷ The Regulation's initial limit was \$100,000 in 1936 and was periodically raised until it reached its current limit of \$5 million.²⁸ Regulation A permitted unregistered public offerings of up to

¹⁸ *Id.* at 28.

¹⁹ Cohn & Yadley, *supra* note 5 at 4-6.

²⁰ *See id.*

²¹ Taylor J. Hart, *Distributing Debt Securities in Cyberspace: How the Internet May Permanently Alter the Role of Underwriters*, 35 SUFFOLK U. L. REV. 395, 403-04 (2001).

²² 17 C.F.R. §§ 23.504-506 (2016).

²³ Gregory C. Smith, *START-UP & EMERGING COMPANIES: PLANNING, FINANCING AND OPERATING THE SUCCESSFUL BUSINESS* § 4.03 (Law Journal Press, 2nd ed. 2015).

²⁴ Siegel, *supra* note 13, at 783.

²⁵ Proposed Rule Amendments for Small and Additional Issues Exemptions Under Section 3(b) of the Securities Act, 79 FR 3926-01 (proposed Jan. 23, 2014) (to be codified at 17 C.F.R. pts. 230, 232, 239, 240 and 260).

²⁶ *Small Business and the SEC*, U.S. SEC. AND EXCHANGE COMMISSION, <https://www.sec.gov/info/smallbus/qasbsec.htm> (last visited Sept. 9, 2016).

²⁷ *Investor Bulletin: Regulation A*, U.S. SEC. AND EXCHANGE COMMISSION, https://www.sec.gov/oiea/investor-alerts-bulletins/ib_regulationa.html (last visited Sept. 9, 2016).

²⁸ Luis A. Aguilar, *Helping Small Business and Protecting Investors*, U.S. SEC. AND EXCHANGE COMMISSION (Mar. 25, 2015), <https://www.sec.gov/news/statement/helping-small-businesses-and-protecting-investors.html>.

\$5 million during a 12-month period by non-reporting U.S. and Canadian companies.²⁹ The Regulation A exemption requires that an offering statement be filed with the SEC.³⁰ That statement must be qualified, which would occur 20 days after its filing without any action from the SEC.³¹ The offering statement must include an offering circular, which is a disclosure document similar to a more condensed version of a prospectus³² that is required when registering a security for sale.³³

Part II

A. The JOBS Act

The JOBS Act was enacted with the primary purpose of helping these emerging companies. The bill is aimed at easing regulations so that it is easier for small businesses to raise capital.³⁴ The JOBS Act had many critics in Congress before passing with bipartisan support. Critics in Congress were concerned that what they called “deregulation” would put investors at a greater risk of fraud.³⁵ To ease the concerns that many had, members of the Senate adopted an amendment to the JOBS Act that placed limits on the amounts that an individual can invest.³⁶

Prior the passing of the JOBS Act, the only legal unregistered ventures in the U.S. was non-equity.³⁷ As a result, investors who gave money to crowdfunded ventures were not able to realize any

²⁹ *Small Business and the SEC*, *supra* note 25.

³⁰ 17 C.F.R. § 230.252 (2016).

³¹ Proposed Rule Amendments of the Securities Act, 79 Fed. Reg. 3926, 3927 (Jan. 23, 2014).

³² *Id.* A prospectus is a preliminary printed statement that describes an enterprise (as a business or publication) and that is distributed to prospective buyers, investors, or participants. *Prospectus Definition*, MERRIAM-WEBSTER, <http://www.merriam-webster.com/dictionary/prospectus> (last visited Sept. 2, 2016).

³³ Jumpstart Our Business Startups Act, Pub. L. No. 112-1-6, 126 Stat. 306 (2012) (codified in various sections of 15 U.S.C.).

³⁴ *Id.*

³⁵ “Jumpstart Our Business Startup Act,” 158 CONG. REC. S1963-77 (daily ed. Mar. 22, 2012).

³⁶ *See id.*

³⁷ Siegel, *supra* note 13, at 778-79.

gain on their investment.³⁸ In order for an investor to profit from his investment, the issuer would have to register with the SEC.³⁹

Emerging Growth Companies

An emerging growth company is an issuer that had less than \$1 Billion in total gross revenue during the previous fiscal year.⁴⁰ An issuer will lose its status as an emerging growth company when: (1) An issuer exceeds \$1 Billion in gross revenue; (2) An issuer reaches its fifth anniversary of the initial IPO; (3) If an issuer issued more \$1 Billion in non-convertible debt during the prior three-year period determined on a rolling basis; or (4) When the issuer is deemed to be a large accelerated filer under the Exchange Act.⁴¹

In order to qualify for the crowdfunding exemption, an issuer must qualify as an emerging growth company.⁴² An issuer must qualify as an emerging growth company at the time of submission in order to submit a registration statement. Once this occurs, an issuer will be considered an emerging growth company for purposes of the provisions in Title I of the JOBS Act.⁴³ Approximately 90 percent of companies going public will qualify as emerging growth companies.⁴⁴

Title I of the JOBS Act creates rules with respect to IPOs, together, these rules are known as “the IPO On-Ramp.”⁴⁵ Under Title I, an emerging growth company does not need to disclose more

³⁸ *Id.* at 779.

³⁹ *Id.*

⁴⁰ JOBS Act, Tit. I, Sec. 101(a).

⁴¹ *Id.*

⁴² Marcus Williams, Donna Cochener, Ryan York and Ryan Maughn, *Current SEC Guidance for “Emerging Growth Companies” Seeking to Take Advantage of the JOBS Act*, DAVIS WRIGHT TREMAINE LLP, (May 30, 2012), <http://www.dwt.com/Current-SEC-Guidance-for-Emerging-Growth-Companies-Seeking-to-Take-Advantage-of-JOBS-Act-05-30-2012>.

⁴³ Jumpstart Our Business Startups Act FAQ, U.S. SEC. AND EXCHANGE COMMISSION (Dec. 21, 2015), <https://www.sec.gov/divisions/corpfin/guidance/cfjjobsactfaq-title-i-general.htm#fn1>.

⁴⁴ Lawrence Hamermesh & Peter Tsoflias, *An Introduction to the Federalist Society’s Panelist discussion titled “Deregulating the Markets: The JOBS Act,”* 38 DE. J. CORP. L. 453, 461 (2013).

⁴⁵ Todd Blakeley Skelton, *2013 Jobs Act Review & Analysis of Emerging Growth Company IPOs*, 15 TENN. J. BUS. L. 455, 456 (2014).

than two years of audited financial statements.⁴⁶ Further, an emerging growth company is not required to submit selected financial data.⁴⁷ In addition, prior to its IPO an emerging growth company can submit to the SEC, in confidence, a draft of its registration statement for review.⁴⁸ This provision allows companies to begin the IPO process without revealing any sensitive business information that would normally be required in the registration statement.⁴⁹ This still however, prohibits a company from making securities offers until the information is publicly disclosed.⁵⁰ If a company decides to complete the IPO process, it must then publicly file its registration statement with the SEC 21 days before the “road show.”⁵¹

As stated above, a company cannot offer a security until it has publicly filed its registration statement with the SEC.⁵² These restrictions prohibit offerings in connection with the IPO before the issuer filed with the SEC.⁵³ This restriction was in place in order to avoid “conditioning the market” prior to an offering.⁵⁴ Now, under the JOBS Act, an emerging growth company can engage in written and oral communications with potential investors provided they are “qualified institutional buyers or institutions that are accredited investors” prior to and after filing the registration statement.⁵⁵

Title II of the JOBS Act

Title II lifts the SEC’s ban on solicitation and advertising for smaller offerings.⁵⁶ Prior to the enactment of Title II, an individual seeking funds from an investor had to have a substantial and pre-

⁴⁶ *Id.* at 459.

⁴⁷ *Id.*; *See, e.g.*, 17 C.F.R. § 229.301 (2016).

⁴⁸ Skelton, *supra* note 44, at 457-58.

⁴⁹ *Id.*

⁵⁰ *Id.*

⁵¹ *Id.* at 458; *See also*, 17 C.F.R. § 230.433(h)(4) (2013).

⁵² *See* JOBS Act, 15 U.S.C § 77b (a)(3) (2012).

⁵³ *Id.*

⁵⁴ Skelton, *supra* note 44, at 460.

⁵⁵ *Id.*

⁵⁶ JOBS Act, 15 U.S.C § 77d (b) (2012).

existing relationship with the individual.⁵⁷ These types of prohibitions were meant to protect potential investors from investing in a company that would ultimately fail.⁵⁸ In order to qualify for this exemption, an individual purchasing a security must be a qualified investor.⁵⁹ A qualified investor is an accredited investor, which consist of banks, broker-dealers, insurance companies, investment companies, and corporations or trusts with assets greater than \$5 million.⁶⁰ Under Title II, an issuer can advertise the offering of a security on the Internet or TV as long as the purchaser is an accredited investor.⁶¹ Many proponents of Title II believe that this is the first step in aiding small businesses' quest to raise capital.⁶² However, companies who do not follow the guidelines set by the SEC are subject to the startup "death sentence." In other words, a company who fails to follow the regulations will be banned from fundraising for a year, which in itself could kill the company.⁶³

Title II also establishes a "Bad Actor" Disqualification.⁶⁴ This disqualification prohibits issuers from participating in exempt securities offerings, if they have been convicted of fraud, or are subject to court or administrative sanctions for securities fraud or other violations.⁶⁵

Title III of the JOBS Act

⁵⁷ Rob Leclerc, *One Year Into Title II Of The JOBS Act*, CRUNCH NETWORK (Oct. 17, 2014), <http://techcrunch.com/2014/10/17/one-year-into-title-ii-of-the-jobs-act/>.

⁵⁸ *Id.*

⁵⁹ *Small Business and the SEC*, *supra* note 25.

⁶⁰ *SEC Implements Title II of the JOBS Act*, MORRISON & FOERSTER LLP (July 11, 2013), <https://media2.mofo.com/documents/130711-sec-implements-title-ii-of-the-jobs-act.pdf>.

⁶¹ Brian Farnkoff, *Crowdfunding For Biotechs: How The SEC's Proposed Rule May Undermine Capital Formation For Startups*, 30 J. CONTEMP. HEALTH L. & POL'Y 131 (Dec. 31, 2013).

⁶² Chance Barnett, *The Crowdfunder's Guide To General Solicitation and Title II of the JOBS Act*, FORBES (Sept. 9, 2013), <http://www.forbes.com/sites/chancebarnett/2013/09/23/the-crowdfunders-guide-to-general-solicitation-title-ii-of-the-jobs-act/print/>.

⁶³ *Id.*

⁶⁴ Jay Baris, David Lynn & Anna Pinedo, *SEC Implements Title II of the JOBS Act*, MORRISON & FOERSTER LLP, <https://media2.mofo.com/documents/130711-sec-implements-title-ii-of-the-jobs-act.pdf>.

⁶⁵ *Id.*

Title III of the Act is also known as the Capital Raising Online While Deterring Fraud and Unethical Non-Disclosure Act of 2012 (“Crowdfund Act”). It regulates how companies can use the crowdfunding method as a way to raise capital. Title III amends Section 4 of the Securities Act of 1933.⁶⁶ It lays out the requirements that intermediaries and issuers need in order to qualify for the Crowdfunding exemption. Title III also creates a new intermediary known as a “crowdfunding portal” that is exempt from registering as a broker.⁶⁷ A crowdfunding portal acting as an intermediary in a transaction for the offer or sale of securities on the behalf of others must register with the SEC.⁶⁸

Title III lays out other numerous rules for registration, disclosures, and conduct of an intermediary.⁶⁹ In January of 2016, the SEC and Financial Industry Regulatory Authority (“FINRA”) rules went into effect, which allowed online funding portals to apply for registration.⁷⁰ An online funding portal acts in the same manner as a broker dealer. Before being able to operate a funding portal must submit information about itself and their business plans to the SEC and FINRA.⁷¹ Additionally, funding portals are required to become members of FINRA, the only qualifying national securities association.⁷²

Since portals will shoulder most of the burden, some question whether companies will get into the portal business.⁷³ Not only are companies subject to the requirements needed to qualify as a registered portal, they also have the burden to protect investors.⁷⁴ A portal must complete background

⁶⁶ CROWDFUND Act, 15 U.S.C § 77d-1 (2012).

⁶⁷ *Id.*

⁶⁸ *Id.*

⁶⁹ *Id.*

⁷⁰ Jeff Zalesin, *Crowdfunding Moves Ahead As Portal Registration Kicks Off*, LAW 360 (Jan. 29, 2016, 4:23 PM ET), <https://www.law360.com/articles/752544>.

⁷¹ *Id.*

⁷² *Id.*

⁷³ See, e.g., Bernadette Tansey, *To Be or Not To Be An Equity Crowdfunding Portal?*, XCONOMY (Nov. 5, 2015), <http://www.xconomy.com/san-francisco/2015/11/05/to-be-or-not-to-be-an-equity-crowdfunding-portal/>.

⁷⁴ Anthony Zeoli, *Why Title III Crowdfunding Remains A Pipe Dream*, LAW 360 (January 25, 2016, 6:10 PM ET), <http://www.law360.com/articles/750648/why-title-iii-crowdfunding-remains-a-pipe-dream>.

checks on issuers and their top executives.⁷⁵ In addition to these background checks, a portal must implement anti-fraud measures, and assess an issuer's commitment to maintaining accurate shareholder records, while educating investors of the potential risks.⁷⁶ Additionally, a portal must affirm that potential investors understand the potential of losing their investment.⁷⁷ All of these requirements come at an expense that forces portals to choose businesses with a high probability of success.⁷⁸

An issuer who offers or sells securities must file with the SEC and provide investors, brokers, and funding portals with material information about the company including but not limited to: the names of the directors and any person holding more than twenty shares of the issuer, a description and anticipated plan of the business, and the financial condition of the business.⁷⁹ Title III also requires greater financial disclosure when issuer seeks more money from investors.⁸⁰ In essence Title III was designed to “help alleviate the funding gap and accompanying regulatory concerns faced by startups and small business in connection with raising capital in relatively small dollar amounts.”⁸¹

Title IV of the JOBS Act

Title IV of the JOBS Act is also known as Regulation A+. Title IV increases the amount of capital a small business can raise from \$5 million to \$50 million.⁸² It limits the securities that may be

⁷⁵ Tansey, *supra* note 72.

⁷⁶ *Id.*

⁷⁷ Thomas James, *Far from the Maddening Crowd: Does the Jobs Act Provide Meaningful Redress to Small Investors for Securities Fraud in Connection with Crowdfunding Operations*, 54 B.C. L. REV. 1767, 1777 (2003), <http://lawdigitalcommons.bc.edu/bclr/vol54/iss4/7>.

⁷⁸ *Id.*

⁷⁹ *See id.* at 1776.

⁸⁰ *See id.*

⁸¹ SEC 78 Fed. Reg. 66430 (proposed Nov. 5, 2013).

⁸² *See* 15 U.S.C. § 77c(b)(2) (2012).

exempt under Regulation A+ to “equity securities, debt securities, and debt securities convertible or exchangeable to equity interest.”⁸³

Since the passing of the JOBS Act, Regulation A, now Regulation A+, was amended to create two offering tiers.⁸⁴ The first tier is for offerings up to \$20 million in a 12-month period.⁸⁵ Tier 1 limits the sales by selling security holders to 30% of the aggregate offering price.⁸⁶ Under Tier 1, an issuer is only required to provide the SEC with information regarding the offering.⁸⁷

Tier 2 is for offerings up to \$50 million in a 12-month period.⁸⁸ Under Tier 2, an issuer is required to limit an unaccredited investor to (1) 10% of the greater of annual income or net worth; or (2) 10 % of the greater of annual revenue or net assets at the end of the fiscal year.⁸⁹ An issuer under tier 2 is subject to greater disclosure requirements. An issuer is required to file semi-annual, annual, and current reports with the SEC.⁹⁰ The annual report must contain almost all of the information disclosed in the original filing statement. Additionally, the financial information in the report requires audited statements.⁹¹

Some companies do not qualify to conduct offerings under Regulation A+. A company who is reporting to the SEC cannot conduct offerings.⁹² In addition to these companies, companies without a business plan or who are registered under the Investment Company Act of 1940 are ineligible to offer securities under Regulation A.⁹³

⁸³ *Id.*

⁸⁴ *See Small Business and the Sec, supra* note 25.

⁸⁵ *Id.*

⁸⁶ *See id.*

⁸⁷ *See* Amendments for Small and Additional Issues Exemptions Under the Securities Act 80 Fed. Reg. 21,812-13 (Apr. 20, 2015) (to be codified at 17 C.F.R. Parts 200, 227, 232, 239, 240, and 249).

⁸⁸ *See id.*

⁸⁹ *See Small Business and the Sec, supra* note 25.

⁹⁰ *See* 17 C.F.R. § 230.257(b)(4) (2015).

⁹¹ *See* 17 C.F.R. § 230.257(b)(2)(i)(A) (2016).

⁹² *See id.*

⁹³ *See id.*

B. Crowdfunding

As defined earlier, crowdfunding is the "practice of funding a project or venture by raising many small amounts of money from a large number of people, typically via the Internet."⁹⁴ Crowdfunding is the combination of two antecedents: crowdsourcing and microlending.⁹⁵ Crowdsourcing is the collections of many contributions from individuals in order achieve a goal.⁹⁶ Essentially, it breaks up what would be an "overwhelming task . . . into smaller chunks so that it becomes . . . feasible."⁹⁷ Microlending⁹⁸ is lending small amounts of money to borrowers who are normally poor.⁹⁹ With crowdfunding, a website, rather than a bank, acts as the intermediary, which some say reduces transactional costs.¹⁰⁰ Generally, there are four types of crowdfunding: equity,¹⁰¹ donation, reward, and debt.¹⁰²

The earliest form of crowdfunding was donation based,¹⁰³ where individuals who give do not expect anything in return for their monetary contribution.¹⁰⁴ Crowdfunding can be dated back to 1997

⁹⁴ *Crowdfunding*, OXFORD DICTIONARIES (2016), <http://www.oxforddictionaries.com/us>; see also Bradford, *supra* note 16, at 10.

⁹⁵ See Bradford, *supra* note 16, at 18.

⁹⁶ See *id.*

⁹⁷ *Id.* at 18.

⁹⁸ Also referred to as microfinancing, which involves lending very small amounts of money to typically poorer borrowers. See *id.* at 18.

⁹⁹ *Id.* at 18-19.

¹⁰⁰ See Robert Steinhoff, *The Next British Invasion Is Securities Crowdfunding: How Issuing Non-Registered Securities Through The Crowd Can Succeed In The United States*, 86 U. COLO. L. REV. 661, 668 (2015).

¹⁰¹ The term crowdfunding throughout this article is in reference to equity crowdfunding, which is when a "company raises financial capital from the crowd in exchange for an ownership stake, represented by share ownership." See *id.* at 671.

¹⁰² See *The Next British Invasion Is Securities Crowdfunding*, *supra* note 99 at 669.

¹⁰³ See *id.*

¹⁰⁴ See *id.*

when a British rock band funded a reunion tour through online donations.¹⁰⁵ ArtistShare¹⁰⁶ became the first platform for crowdfunding in in the early 2000s, with others following in the coming years.¹⁰⁷

A question concerning crowdfunding that was frequently asked was: Is a crowdfunding investment a security? A Security is “any note, stock, treasury stock, security future, security-based swap, bond, debenture, evidence of indebtedness, certificate of interest or participation in any profit-sharing agreement, collateral-trust certificate, preorganization certificate or subscription, transferable share, investment contract, voting-trust certificate, certificate of deposit for a security....”¹⁰⁸ Steven Bradford suggests, that it should be considered a security if crowdfunding sites are selling investment contracts.¹⁰⁹ In *SEC v. Howey*, the court uses a four-part test to determine if an investment would be a security.¹¹⁰ If an issuer were offering interest, it would be considered an investment contract, but if investors only receive a return of their principal it would not.¹¹¹

The median amount raised through crowdfunding was \$28,583, with the largest amount being \$82 Million.¹¹² Crowdfunding tripled from \$530 million in 2009, to over \$1.5 billion in 2011.¹¹³ In 2012, President Obama signed the Jumpstart Our Business Startups Act (“JOBS”) into law.¹¹⁴ The JOBS Act allows emerging companies to solicit funds via crowdfunding platforms.¹¹⁵ Businesses begin

¹⁰⁵ Dean Golemis, *British Band's U.S. Tour Is Computer-generated*, CHI. TRIB. (Sept. 23, 1997), http://articles.chicagotribune.com/1997-09-23/features/9709230071_1_music-fans-newsgroup-marillion.

¹⁰⁶ ArtistShare was founded by Brian Camelio. See David M. Freedman & Matthew R. Nutting, *A Brief History of Crowdfunding: Including Rewards, Donation, Debt, and Equity Platforms in the USA*, FREEDMAN-CHICAGO.COM (June 22, 2015), <http://www.freedman-chicago.com/ec4i/History-of-Crowdfunding.pdf>.

¹⁰⁷ *Id.*

¹⁰⁸ JOBS Act, 15 U.S.C. § 77b(a)(1) (2012).

¹⁰⁹ Bradford, *supra* note 16, at 30.

¹¹⁰ *SEC v. Howey Co.*, 328 U.S. 293, 298-99 (1946) (An investment contract is (1) an investment of money (2) in a common enterprise (3) with an expectation of profits (4) arising solely from the efforts of the promoter or a third party).

¹¹¹ See *Small Business and the SEC*, *supra* note 25.

¹¹² *Id.*

¹¹³ *Id.*

¹¹⁴ Jumpstart Our Business Startups (JOBS) Act Pub. L. No. 112-106, 126 Stat. 306 (2012) (codified in various sections of 15 U.S.C.); Mark Landler, *Obama Signs Bill to Promote Start-Up Investments*, NEW YORK TIMES (Apr. 5, 2012), <http://www.nytimes.com/2012/04/06/us/politics/obama-signs-bill-to-ease-investing-in-start-ups.html>.

¹¹⁵ Freedman & Nutting, *supra* note 105 at 7.

the process by requesting funds on a crowdfunding site. Businesses will disclose a business plan, the product, and describes how they will use the funds.¹¹⁶

Types of Crowdfunding

1. Equity Crowdfunding:

In equity-based crowdfunding, an investor receives a stake in the company they are investing in. Investors normally invest in small or emerging businesses that have a high potential of growth, but lack the capital to do so.¹¹⁷ Often investors are not motivated by near term returns.¹¹⁸ Instead investors can be motivated to invest because of shared values, or because a business is creating jobs in the investor's community.¹¹⁹

2. Debt-Based Crowdfunding:

Also known as lending-based, this type of crowdfunding allows businesses to incur debt to raise money using crowdfunding platforms.¹²⁰ With debt crowdfunding, an investor invests in a security of the company.¹²¹ With these, investors negotiate a fixed repayment term and are paid a specific interest during the term of the loan.¹²² Debt crowdfunding makes it easier for financial planning because of the fixed return.¹²³ Some suggest that debt crowdfunding is a type of security.¹²⁴ Some forms of debt crowdfunding offer notes, which would be considered securities.¹²⁵ If a

¹¹⁶ Bradford, *supra* note 16, at 30.

¹¹⁷ Steinhoff, *supra* note 99, at 671.

¹¹⁸ Kristof De Buysere et al., *A Framework for European Crowdfunding*, 11 (2012), <http://www.fundraisingschool.it/wp-content/uploads/2013/02/European-Crowdfunding-Framework-Oct-2012.pdf>.

¹¹⁹ *Id.* at 12.

¹²⁰ *Id.* at 10.

¹²¹ Jason Futko, *Equity v. Debt Crowdfunding*, CROWDFUND INSIDER (Sept. 24, 2014, 9:49 AM), <http://www.crowdfundinsider.com/2014/09/50628-equity-vs-debt-crowdfunding>.

¹²² *Id.*

¹²³ *Id.*

¹²⁴ Bradford, *supra* note 16, at 6.

¹²⁵ *Id.*

crowdfunding site offers a note that pays the investor interest, then it would be considered a security under the test formed in *Reves v. Ernst & Young*.¹²⁶

3. Rewards-Based Crowdfunding

Unlike equity and debt-based Crowdfunding, investors do not see a return on their investment. Instead investors receive a reward or perk for their investment.¹²⁷ The reward is usually based on the amount an individual contributes.¹²⁸ These rewards usually consist of a product or service from the company, like a ticket to a movie premier or signed memorabilia.¹²⁹ This allows the person seeking the funds to keep 100% ownership of his or her company or project without having incurred any debt.¹³⁰

C. The SEC Rules for Crowdfunding

The SEC rules, implementing the JOBS Act, are intended to “align crowdfunding transactions under Section 4(a)(6) with the central tenets of the original concept of crowdfunding.”¹³¹ The SEC refers to these rules as Regulation Crowdfunding (hereinafter “SEC Rules”).¹³² The SEC Rules set the rules that govern the offer and sale of securities pursuant to the JOBS Act.¹³³ The rules also set guidelines for the regulation of registered funding portals and broker dealers that issuers are required to use intermediaries in the offer and sale of securities.¹³⁴ The JOBS Act creates a crowdfunding exemption, as discussed above and prescribes specific requirements needed to qualify for this exemption.¹³⁵

¹²⁶ *Id.*; *See also*, *Reves v. Ernst & Young*, 494 U.S. 56, 67 (1990).

¹²⁷ Marc Zorn, *What is reward based crowdfunding?*, VISION LAUNCH, (June 29, 2015), <http://www.visionlaunch.com/what-is-rewards-based-crowdfunding/>.

¹²⁸ *Id.*

¹²⁹ *Id.*

¹³⁰ *See* Freedman & Nutting, *supra* note 105 at 2-3.

¹³¹ Crowdfunding, 78 Fed. Reg. 66428, 66430 (Feb. 3, 2014) (to be codified at 17 C.F.R. pt. 200, 227, 232, 239 & 249).

¹³² 17 C.F.R. § 227.100 (2016).

¹³³ 17 C.F.R. § 227.100(a) (2016).

¹³⁴ 17 C.F.R. § 227.100 (2016).

¹³⁵ *Id.*

1. Limits on Capital Raise

One of the requirements to qualify for this exemption is a limit on the dollar amount of the securities that may be sold by an issuer within a 12-month period.¹³⁶ The SEC Rules places a \$1 million limit on the aggregate amount sold to all investors.¹³⁷ However, capital raised through other exempt transaction will not be counted when determining the aggregate amount sold in reliance on Section 4(a)(6).¹³⁸ In adopting this rule the SEC explained that it is consistent with the statute and provides for a “meaningful addition to the existing capital formation options for smaller companies while maintaining important investor protections.”¹³⁹

2. Investment Limits

The SEC Rules also limit how much an investor can invest in a company while still being able to qualify for the exemption. An investor will be limited to investing “(1) the greater of: \$2,000 or 5 percent of the lesser of the investor’s annual income or net worth if either annual income or net worth is less than \$100,00; or (2) 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 annual income and net worth are \$100,000 or more.”¹⁴⁰ The SEC recognized that this rule could restrict capital formation, but also recognized that it could minimize an investor’s exposure to risks.¹⁴¹

3. Transactions Conducted Through an Intermediary

Rule 100(a)(3) provides that in “any transaction conducted in reliance on Section 4(a)(6), an issuer may use only one intermediary.”¹⁴² Additionally, the transaction must be conducted exclusively

¹³⁶ 17 C.F.R. § 227.100(a)(1) (2016).

¹³⁷ *Id.*

¹³⁸ *Id.*

¹³⁹ Crowdfunding, 80 Fed. Reg. 71388, 71391 (Nov. 16, 2015).

¹⁴⁰ 17 C.F.R. § 227.100(a)(2) (2016).

¹⁴¹ Crowdfunding, 80 Fed. Reg. at 71394.

¹⁴² Crowdfunding, 80 Fed. Reg. at, 71395.

on the intermediary’s platform.¹⁴³ The rule also defines platform as “an Internet website or other similar electronic medium through which a registered broker or a registered funding portal acts as an intermediary in a transaction involving the offering or sale of securities in reliance on Section 4(a)(6).”¹⁴⁴

4. Exclusion of Certain Issuers from Eligibility under Section 4(a)(6)

Certain issuers are excluded from eligibility for the crowdfunding exemption: issuers that are not organized under the laws of a state or territory of the U.S., or District of Columbia; issuers that are subject to Exchange Act reporting requirements; Investment companies as defined in the Investment Company Act of 1941¹⁴⁵ or companies that are excluded from the definition of investment company under Section 3(b) or 3(c) of the Investment Company Act; and any other issuer that the Commission, by rule or regulation, determines appropriate.¹⁴⁶ Rule 100(b) of the SEC Rules excludes the categories of issuers identified in Section 4A(f).¹⁴⁷ In addition to the exclusions in Section 4A(f), Rule 100(h) spells out others who are disqualified: (1) issuers that are disqualified from relying on Section 4(a)(6) pursuant to the disqualification provision in Rule 503(a) of the SEC Rules; (2) issuers that have sold securities in reliance on Section 4(a)(6) if they have not filed with the Commission and provided to investors, to the extent required, the ongoing annual reports required by the SEC Rules during the two years immediately preceding the filing of the required new offering statement; and (3) issuers that have no specific business plan or that have indicated that their business plan is to engage in a merger or acquisition with an unidentified company or companies.¹⁴⁸

5. Issuer Requirements

¹⁴³ 17 C.F.R. § 227.100(a)(3) (2016).

¹⁴⁴ Crowdfunding, 80 Fed. Reg. at, 71395.

¹⁴⁵ 15 U.S.C. § 80a-3 (2016).

¹⁴⁶ 17 C.F.R. § 227.100(b)(1-3) (2016).

¹⁴⁷ 17 C.F.R. § 243.100(b) (2016).

¹⁴⁸ 17 C.F.R. § 227.100(b)(1-6) (2016).

Under Rule 201, an issuer is required to disclose information about its directors, officers, legal status and 20 percent Beneficial Owners.¹⁴⁹ Information about the director and officer's business experience must cover the previous three years.¹⁵⁰ An issuer under Rule 201(d) is required to disclose information about its business and business plan.¹⁵¹ The Rule does not require an issuer to disclose this information with specificity or in great detail. In their reasoning, the SEC explained that the lack of specifics will allow for flexibility as issuers develop their business.¹⁵²

6. Use of Proceeds

Under Rule 201(i), an issuer must disclose the purpose of the offering and how the issuer intends to use the proceeds.¹⁵³ The SEC states that this rule is intended to provide investors with information to evaluate their investment. Under this rule, the SEC gives the issuer discretion as to what information it has to release.¹⁵⁴

7. Target Offering Amount and Deadline

Section 4A(b)(1)(F) of the Securities Act requires issuers to disclose the target offering amount and the deadline to reach the target.¹⁵⁵ SEC Rule 200(g) requires an issuer to disclose if they would accept investments over the target amount.¹⁵⁶ The Rule also requires that issuers at the commencement of the offering disclose the maximum amount they would accept.¹⁵⁷ Rule 200(j) requires an issuer to describe the process to cancel an investment commitment or to complete the

¹⁴⁹ 17 C.F.R. § 227.201(b) (2016).

¹⁵⁰ 17 C.F.R. § 227.201(b).

¹⁵¹ 17 C.F.R. § 227.201(d).

¹⁵² SEC Proposed Crowdfunding Regulation, 78 Fed. Reg. 66457 (proposed Nov. 5, 2013).

¹⁵³ 17 C.F.R. § 227.201(i).

¹⁵⁴ 17 C.F.R. § 227.201(i).

¹⁵⁵ Securities Act of 1933 §4A(b)(1)(F).

¹⁵⁶ 17 C.F.R. § 227.201(g).

¹⁵⁷ 17 C.F.R. § 227.201(h).

transaction once the target amount is met.¹⁵⁸ Under the rules, an issuer may close the offering prior to the deadline if it provides at least five business days' notice.¹⁵⁹

Part III—Issues with the JOBS Act

A common theme among critics of the JOBS Act, specifically Title III is that there is a greater possibility of fraud. It is pointed out that one reason for fraud is that investors do not have personal contact or knowledge of the business idea besides what its presented on the funding portal.¹⁶⁰ The fear is that new investors, who are less wealthy than the traditional investors will be exposed to unknown financial risks, and therefore fraud.¹⁶¹ Many believe that the eased regulations would result in an increase in fraud. One critic suggests, “[f]raudsters will use crowdfunding sites to deceive investors and take their money.”¹⁶² However, it is recognized that the possibility a greater fraud is not exclusive to the exemptions provided in the JOBS Act.¹⁶³

Currently, under §201(h), an issuer must disclose if they would accept any funds over the target amount.¹⁶⁴ Under these rules, an issuer is setting two target amounts.¹⁶⁵ The issue with this rule is that the SEC does not require the issuer to disclose its reasons for accepting funds in excess of its original target amount. The SEC states that it believes investors in a crowdfunding transaction will benefit from clear disclosure.¹⁶⁶ However, the rules, specifically Rule 200(h), lack the type of disclosure that is beneficial to investors.

¹⁵⁸ 17 C.F.R. § 227.201(j)(1)-(2).

¹⁵⁹ *Id.*

¹⁶⁰ *See* Buysere et al., *supra* note 117 at 15.

¹⁶¹ *See* James, *supra* note 76, at 1767.

¹⁶² *See* Bradford, *supra* note 16.

¹⁶³ *Id.* Bradford argues that more securities offering will result in more fraud.

¹⁶⁴ 17 C.F.R. § 227.201(h).

¹⁶⁵ *See* Tansey, *supra* note 72.

¹⁶⁶ SEC Proposed Crowdfunding Regulation, 78 Fed. Reg. 66457 (proposed Nov. 5, 2013).

Some critics of the JOBS Act say that though the bill is intended to promote the growth of small businesses, it is doing so at the expense of investor protection.¹⁶⁷ Andrew Sorkin, a financial commentator points to the lack of transparency as a key factor that could lead to substantial losses for investors.¹⁶⁸ Sorkin notes that issuers and the SEC would be involved in secretive conversations about what to disclose and that information would not be available until twenty-one days before the offering.¹⁶⁹ Sorkin also looks at Groupon's IPO.¹⁷⁰ Five months after the IPO, investors lost approximately forty-one percent of their investments.¹⁷¹ Sorkin attributes the loss to accounting irregularities and losses before the company went public. Sorkin suggests that had Groupon sought investors under the JOBS Act the "red flags" would have been less evident.

Other critics of the JOBS Act agree with Sorkin that the lack of transparency is an issue. As J. Edward Ketz¹⁷² put it: "I find it amazing that Congress would allow any firm to work behind closed doors on any accounting or auditing issue."¹⁷³ Michael Rapoport says that this closed door provision might have prevented investors from learning of Groupon's accounting issues until after they had been resolved.¹⁷⁴

Part IV

The criticisms and concerns that come with the JOBS Act and Regulation Crowdfunding are warranted. It is clear based on the commentary from critics that Crowdfunding is not viable in its

¹⁶⁷ Andrew Ross Sorkin, *JOBS Act Jeopardizes Safety Net for Investors*, N.Y. TIMES: DEALBOOK (Apr. 2, 2012), http://dealbook.nytimes.com/2012/04/02/jobs-act-jeopardizes-safety-net-for-investors/?_r=0.

¹⁶⁸ *Id.*

¹⁶⁹ *Id.*

¹⁷⁰ Initial Public Offering, INVESTOPEDIA, <http://www.investopedia.com/terms/i/ipo.asp> (last visited Aug. 29, 2016).

¹⁷¹ Sorkin, *supra* note 166.

¹⁷² J Edward Ketz is an associate professor of accounting at Penn State University (*see* http://php.smeal.psu.edu/smeal/dirbio/displayBio.php?t_user_id=k55).

¹⁷³ Michael Rapoport, *In Wake of Groupon Issues, Critics Wary of JOBS Act*, WALL STREET JOURNAL (Apr. 2012), <http://www.wsj.com/articles/SB10001424052702304023504577317932455874856>.

¹⁷⁴ *Id.*

current form. Critics on one side have recognized that the exemptions for disclosure open the door for greater amounts of fraud.¹⁷⁵ Conversely, other critics believe that the rules will only make it harder for small businesses to raise a meaningful amount of capital.¹⁷⁶

It is obvious that when looking at the purposes of the JOBS Act and the new SEC rules that the two are in conflict. Rather than implementing the JOBS Act, the SEC rules hinder its purpose. As previously discussed, the purpose of the JOBS Act is to make it easier for small businesses to raise funds, yet the new rules, which are aimed at protecting investors, make it hard for businesses to raise funds.¹⁷⁷ Because of this conflict, it would be fair to conclude that Congress must decide between the JOBS Act and the new SEC Rules. However, Congress does not need to make such a decision, but since there is a clear need for successful small businesses, Congress should slightly favor small business at little expense to investors. Congress should mandate that the SEC ease some of these rules. It is recognizable that some critics of these exemptions would decry the notion of more exemptions, saying that fraud is then inevitable. However, choosing the JOBS Act over the rules will not put investors at a greater risk of fraud if the SEC implements the right rules.

First, the monetary threshold in order to qualify for the exemptions under the JOBS Act should be lower. This would require Congress to redefine an emerging growth company.¹⁷⁸ Currently, the threshold is no more than \$1 Billion in total gross revenue.¹⁷⁹ An emerging growth company has some of the same characteristics as a start-up company. Both are fairly new companies, with lower revenues and fewer employees.

¹⁷⁵ See, e.g., Joan MacLeod Heminway & Sheldon Ryan Hoffman, *Proceed at Your Peril; Crowdfunding and the Securities of 1933*, 78 TENN. L. REV. 879, 935.

¹⁷⁶ See, e.g., Zeoli, *supra* note 73.

¹⁷⁷ *Id.*

¹⁷⁸ “Jumpstart Our Business Startup Act,” 158 CONG. REC. S1963-77 (daily ed. Mar. 22, 2012).

¹⁷⁹ *Id.*

Alex Wilhelm, a technology analyst, uses a 50-100-500 rule to determine if a company is a startup.¹⁸⁰ The rule is: \$50 Million in total revenue; 100 or more employees; or worth more than \$500 Million on paper.¹⁸¹ He notes, “If your company has, or is any of the following, you have to hang up your startup uniform.”¹⁸² When looking at this definition of a startup, it seems that the \$1 Billion cap is excessive. Congress should use a model similar to Wilhelm’s to determine what qualifies as an emerging growth company. This new definition of an emerging growth company could then be used to determine who qualifies for the exemptions under the JOBS Act.

Although there are exemptions that seemingly make it easier for small businesses to raise capital, these exemptions do not go far enough. The only way to ease these regulations while simultaneously protecting investors is for Congress to make it more difficult for businesses to qualify for the exemptions. While this may seem to be counterintuitive, such a solution could be feasible with two approaches.

The first approach would be a tiered approach. Here, exemptions would be based on tiers. Businesses would qualify for different tiers based on the number of employees, the company’s total revenue, and the amount the company seeks to raise. The smaller the company and the smaller the amount, more exemptions apply. The larger the company and the amount fewer exemptions would apply.

The second approach would make it more difficult for businesses to qualify for the exemptions. This approach would restrict the number of companies that qualify for the exemption, by lowering the amount of total revenue needed to determine an emerging growth company. This

¹⁸⁰ Alyson Shontell, *This is The Definitive Definition of A Startup*, *Business Insider*, BUSINESSINSIDER (Dec. 31, 2014), <http://www.businessinsider.com/what-is-a-startup-definition-2014-12>.

¹⁸¹ *Id.*

¹⁸² *Id.*

approach would significantly raise the cap, or eliminate the cap on the amounts that companies are allowed to raise while eliminating the cap on the amounts investors can give.

Although the changes articulated above would better facilitate growth in small business, it cannot be done without Congress changing the requirements of intermediaries. Critics have recognized that it is difficult and time consuming for portals to comply with the requirements under Title III.¹⁸³ Furthermore, these requirements unfairly shift the burden of protecting investors on to the portals.¹⁸⁴ While funding portals should still have some obligations, what obligations they have should be lessened. Under Title II, portals have some obligations, but are not affirmatively required like they are under Title III.¹⁸⁵

The two approaches discussed above may be helpful to the growth of businesses, but the concern for investor protection is still present. The new SEC Rules allow issuers to raise more than their target amount. The SEC Rules require an issuer to disclose how the funds exceeding the target amount will be used.¹⁸⁶ This article however, proposes that the SEC eliminate the possibility of raising any funds in excess of an issuer's stated target amount. The new approach would make it easier for businesses to raise capital, so the need for excess capital in a 12-month period would be gone. Eliminating the possibility that a company will raise more than what it seeks could be beneficial to the goal of protecting investors from the potential of greater loss and fraud.

Currently, an issuer can sell an aggregate of \$1 Million to investors in a 12-month period. With the new approaches suggested here, the only cap within a 12-month period would be the issuer's target amount. It is recognizable that having free reign to raise as much money as an issuer wishes is controversial. Therefore, the SEC would have to place an overall cap on the overall amount of money

¹⁸³ Zeoli, *supra* note 73.

¹⁸⁴ *Id.*

¹⁸⁵ *Id.*

¹⁸⁶ 17 C.F.R. § 227.201(i) (2015).

a business can raise during the life of the exemption. The question would then be: how long would a company be eligible for the exemption?

This article presents two approaches for answering that question. The first would be that a company is eligible for the exemption as long as it is considered an emerging growth company. The second, and probably more controversial approach would be to limit the exemption to a 12 or 24-month period. The latter approach would have a two-fold effect. First, it would stay consistent with the main purpose of the JOBS Act, as it would jumpstart small business growth by providing greater access to capital. Currently, as is, the SEC Rules does more than jumpstart small businesses; they sustain them. Second, this approach would greatly protect investors by limiting them to a one-time investment in companies with high risks. This would benefit funding portals as well, because it would ease the burden of “babysitting” issuers and investors to a relatively short period. It would also make a funding portal more profitable since a shorter offering period would lessen the expense of protecting an investor with each offering.

Lastly, Congress should remove the provision that allows the SEC and issuers to discuss material information behind closed doors. It is recognized that this provision may be intended to protect the issuer, but it also puts the investor at a disadvantage. One of the differences between the JOBS Act exemption and a regular IPO is that an issuer that is eligible for the exemption does not have to disclose the same amount of information as a company that is not exempt. What little information that an issuer is required to release should be released without prior involvement of the SEC. One commentator suggested that in order to effectively protect investors from fraud is to compel issuers to release sufficient information so that investors can make informed decisions.¹⁸⁷ In addition to eliminating these secret conversations, an issuer should release material information 2 to

¹⁸⁷ See James, *supra* note 76, at 1775.

3 times during the offering period.¹⁸⁸ This would allow investors to make informed decisions when investing. It will also again ease the burden that the SEC places on funding portals.

CONCLUSION

It would be beneficial for the American economy if there is a growth in small businesses. For the most part, the JOBS Act gives small business a channel through crowdfunding. But the Act, as well intentioned as it is, has its flaws. The implementations of the SEC Rules are in place to protect investors at the cost of small business growth. While investor protection is important, it must be balanced with small business growth. This article offers solutions that will balance the two. While the approaches offered here are not yet perfected, it takes the necessary steps of protecting investors while giving small businesses the channel to easily raise capital.

¹⁸⁸ *Id.* This would largely depend on the length of the issuing period.