

University of Tennessee College of Law

Legal Scholarship Repository: A Service of the Joel A. Katz Law Library

Scholarly Works

Faculty Work

2014

How Congress Killed Investment Crowdfunding: A Tale of Political Pressure, Hasty Decisions, and Inexpert Judgments That Begg for a Happy Ending

Joan MacLeod Heminway
University of Tennessee College of Law

Follow this and additional works at: https://ir.law.utk.edu/utklaw_facpubs



Part of the [Law Commons](#)

Recommended Citation

Heminway, Joan MacLeod, "How Congress Killed Investment Crowdfunding: A Tale of Political Pressure, Hasty Decisions, and Inexpert Judgments That Begg for a Happy Ending" (2014). *Scholarly Works*. 817.
https://ir.law.utk.edu/utklaw_facpubs/817

This Article is brought to you for free and open access by the Faculty Work at Legal Scholarship Repository: A Service of the Joel A. Katz Law Library. It has been accepted for inclusion in Scholarly Works by an authorized administrator of Legal Scholarship Repository: A Service of the Joel A. Katz Law Library. For more information, please contact eliza.boles@utk.edu.

University of Tennessee College of Law

Legal Scholarship Repository: A Service of the Joel A. Katz Law Library

UTK Law Faculty Publications

2014

How Congress Killed Investment Crowdfunding: A Tale of Political Pressure, Hasty Decisions, and Inexpert Judgments That Begg for a Happy Ending

Joan M. Heminway

Follow this and additional works at: https://ir.law.utk.edu/utklaw_facpubs



Part of the [Law Commons](#)



DATE DOWNLOADED: Wed Apr 20 13:34:53 2022

SOURCE: Content Downloaded from [HeinOnline](https://heinonline.org)

Citations:

Bluebook 21st ed.

Joan MacLeod Heminway, How Congress Killed Investment Crowdfunding: A Tale of Political Pressure, Hasty Decisions, and Inexpert Judgments That Begg for a Happy Ending, 102 KY. L.J. 865 (2013).

ALWD 7th ed.

Joan MacLeod Heminway, How Congress Killed Investment Crowdfunding: A Tale of Political Pressure, Hasty Decisions, and Inexpert Judgments That Begg for a Happy Ending, 102 Ky. L.J. 865 (2013).

APA 7th ed.

Heminway, J. (2013). How congress killed investment crowdfunding: tale of political pressure, hasty decisions, and inexpert judgments that begg for happy ending. Kentucky Law Journal, 102(4), 865-890.

Chicago 17th ed.

Joan MacLeod Heminway, "How Congress Killed Investment Crowdfunding: A Tale of Political Pressure, Hasty Decisions, and Inexpert Judgments That Begg for a Happy Ending," Kentucky Law Journal 102, no. 4 (2013-2014): 865-890

McGill Guide 9th ed.

Joan MacLeod Heminway, "How Congress Killed Investment Crowdfunding: A Tale of Political Pressure, Hasty Decisions, and Inexpert Judgments That Begg for a Happy Ending" (2013) 102:4 Ky LJ 865.

AGLC 4th ed.

Joan MacLeod Heminway, 'How Congress Killed Investment Crowdfunding: A Tale of Political Pressure, Hasty Decisions, and Inexpert Judgments That Begg for a Happy Ending' (2013) 102(4) Kentucky Law Journal 865

MLA 9th ed.

Heminway, Joan MacLeod. "How Congress Killed Investment Crowdfunding: A Tale of Political Pressure, Hasty Decisions, and Inexpert Judgments That Begg for a Happy Ending." Kentucky Law Journal, vol. 102, no. 4, 2013-2014, pp. 865-890. HeinOnline.

OSCOLA 4th ed.

Joan MacLeod Heminway, 'How Congress Killed Investment Crowdfunding: A Tale of Political Pressure, Hasty Decisions, and Inexpert Judgments That Begg for a Happy Ending' (2013) 102 Ky LJ 865

Provided by:

University of Tennessee College of Law Joel A. Katz Law Library

-- Your use of this HeinOnline PDF indicates your acceptance of HeinOnline's Terms and Conditions of the license agreement available at

<https://heinonline.org/HOL/License>

-- The search text of this PDF is generated from uncorrected OCR text.

How Congress Killed Investment Crowdfunding: A Tale of Political Pressure, Hasty Decisions, and Inexpert Judgments that Begs for a Happy Ending

Joan MacLeod Heminway¹

EVEN promising small businesses have trouble finding friends—and-family, seed, angel, and venture capital in sufficient quantities to allow them to succeed and thrive. By 2011, a number of small businesses had been successful in raising donated funds and other funding by taking their capital appeals to the Internet.² Instead of asking interested people to “like” their Facebook page, “follow” them on Twitter, or accept an invitation to “connect” on LinkedIn (i.e., “link in” with them), entrepreneurs³ had begun to ask people to like, follow, and connect with them by funding a project or business through appeals made over the Internet using social networking and e-commerce based technologies.⁴ Crowdfunding was born and began to get traction as a business financing option.

Legally, entrepreneurs could not offer or sell a profit-sharing or revenue-sharing interest in the project or business for which they sought funding unless the offering was registered under the Securities Act of 1933, as amended (the “1933 Act”).⁵ Instruments embodying that type of interest are typically deemed to be securities under federal or state law (or both).⁶ The offer or sale of a security requires registration with federal or state authorities unless

1 W.P. Toms Distinguished Professor of Law, The University of Tennessee College of Law. New York University School of Law, J.D. 1985; Brown University, A.B. 1982.

2 See Suw Charman-Anderson, *Crowdfunding Raised \$1.5bn in 2011, Set to Double in 2012*, FORBES (May 11, 2012, 11:20 AM), <http://www.forbes.com/sites/suwcharmananderson/2012/05/11/crowdfunding-raised-1-5bn-in-2011-set-to-double-in-2012/>; Joachim Hemer, *A Snapshot on Crowdfunding* 22 (Fraunhofer Inst. for Sys. & Innovation Research ISI, Working Papers Firms & Region No. R2/2011, 2011), available at http://www.isi.fraunhofer.de/isi-media/docs/p/de/arbapap_unternehmen_region/ap_r2_2011.pdf.

3 The term “entrepreneur” is used here broadly to refer to those seeking funding for a business or product.

4 See, e.g., SHERWOOD NEISS ET AL., CROWDFUND INVESTING FOR DUMMIES 30–31 (2013) (outlining attributes of the internet and social media environment in which crowdfund investing originated and evolved); THOMAS ELLIOTT YOUNG, THE EVERYTHING GUIDE TO CROWDFUNDING 103–18 (2013) (describing social media and e-commerce applications for potential use in crowdfunding).

5 See Joan MacLeod Heminway & Shelden Ryan Hoffman, *Proceed at Your Peril: Crowdfunding and the Securities Act of 1933*, 78 TENN. L. REV. 879, 906–07, 911–21 (2011) (explaining the registration and exemption provisions of the 1933 Act in context).

6 See *id.* at 885–906 (describing and explaining the definition of a security under the 1933 Act and applying it to crowdfunding).

an exemption is available.⁷ Then—existing exemptions under federal and state law did not permit broad-based solicitations of investors over the Internet.⁸

Despite the success of some entrepreneurs in raising funds over the Internet through crowdfunding that avoided the sale of securities, a number of entrepreneurs desired to offer funders some pecuniary benefit—some financial “skin in the game.” Specifically, they wanted to be able to offer and sell equity, interest-bearing debt instruments, and other profit-sharing or revenue-sharing instruments to the Internet crowd.⁹ Momentum began to build for a federal exemption from 1933 Act registration for crowdfunded securities. President Obama indicated his encouragement for a solution in the fall of 2011 by including crowdfunding support in the American Jobs Act¹⁰ and backing the original investment crowdfunding bill filed in the U.S. House of Representatives soon afterward.¹¹ Lobbying from various quarters became more and more intense, and coalitions were formed to push the initiative forward.¹² By the spring of 2012, the clamoring for investment crowdfunding (also known as securities crowdfunding and crowdfund investing) reached a veritable crescendo.¹³ With the President out in front of the issue and diffuse bipartisan support, Congress no doubt believed it had to act—and, thus, it did act. Both Houses passed the Capital Raising Online While Deterring Fraud and Unethical Non-Disclosure Act (the “CROWDFUND Act”) as Title III of the Jumpstart Our Business Startups Act (“JOBS Act”)¹⁴ in March 2012,¹⁵

7 Securities Act of 1933, 15 U.S.C. § 77e (2012).

8 See C. Steven Bradford, *Crowdfunding and the Federal Securities Laws*, 2012 COLUM. BUS. L. REV. 1, 44–48; Heminway & Hoffman, *supra* note 5, at 916, 920–21; Brook Knight et al., *A Very Quiet Revolution: A Primer on Securities Crowdfunding and Title III of the Jobs Act*, 2 MICH. J. PRIVATE EQUITY & VENTURE CAP. L. 135, 135 (2012) (“Until the recent passing of the Jumpstart Our Business Startups Act . . . , however, there was no legal way for businesses to tap this network to offer a financial interest (either as debt or equity) to the public without registering the offering with the Securities and Exchange Commission . . .”).

9 See NEISS ET AL., *supra* note 4, at 34–35.

10 See Press Release, Office of the White House Press Sec’y, Fact Sheet: The American Jobs Act (Sept. 8, 2011), *available at* <http://www.whitehouse.gov/the-press-office/2011/09/08/fact-sheet-american-jobs-act>.

11 See Executive Office of the President, Statement of Administration Policy (Nov. 2, 2011), *available at* http://www.whitehouse.gov/sites/default/files/omb/legislative/sap/112/saphr2930r_20111102.pdf (“The Administration supports House passage of H.R. 2930.”).

12 See NEISS ET AL., *supra* note 4, at 37–38.

13 See, e.g., Sarah Lai Stirland, *Lobbying 2.0: Crowdfunding Act Buoyed by the Enthusiasm of the Crowds*, TECHPRESIDENT (Mar. 14, 2012), <http://techpresident.com/news/21907/lobbying-20-crowdfunding-act-buoyed-enthusiasm-crowds> (describing the lobbying effort).

14 Jumpstart Our Business Startups (JOBS) Act, Pub. L. No. 112–106, 126 Stat. 306 (2012). This Article uses the acronym “CROWDFUND” for Title III of the JOBS Act, after the short title given to this Title by Congress: Capital Raising Online While Deterring Fraud and Unethical Non-Disclosure Act. Title III of the JOBS Act can be found at Pub. L. No. 112–106, §§ 301–305, 126 Stat. 306, 315–23 (2012) [hereinafter CROWDFUND Act].

15 Ed O’Keefe, *House Passes JOBS Act, Sends Bill to Obama*, WASH. POST (Mar. 27, 2012, 3:10 PM), <http://www.washingtonpost.com/blogs/2chambers/post/house-passes-jobs-act-sends-bill->

which the President signed into law in the first week of April.¹⁶ The U.S. Securities and Exchange Commission (“SEC”) was compelled to promulgate enabling regulation to effectuate the CROWDFUND Act;¹⁷ the lobbyists engaged in back-slapping—accompanied by attaboys and hazzahs—and took visible credit;¹⁸ and from all public appearances, the future of investment crowdfunding looked rosy. The honeymoon period was not, however, uniformly experienced, and in any event, it did not last long.

The SEC’s rulemaking was slow in coming, missing the target date set in the CROWDFUND Act.¹⁹ During this period of delay, commentators routinely denounced the postponement and expressed fear that the SEC’s rulemaking would unduly limit investment crowdfunding.²⁰ Yet, as this Article demonstrates, it is principally the U.S. Congress that has limited the capacity of the CROWDFUND Act to foster capital formation for small businesses through investment crowdfunding.²¹ The provisions of the CROWDFUND Act, as enacted by Congress, create a significant cost structure that is not likely to be outweighed by the benefits of a crowdfunded offering conducted under the Act; some commentators have realized this and reported it correctly.²²

to-obama/2012/03/27/gIQA9DfZeS_blog.html (reporting final congressional action on the JOBS Act).

16 E.g., Mark Landler, *Obama Signs Bill to Promote Start-Up Investments*, N.Y. TIMES (Apr. 5, 2012), <http://www.nytimes.com/2012/04/06/us/politics/obama-signs-bill-to-ease-investing-in-start-ups.html> (reporting the signing of the JOBS Act into law).

17 Each section of the CROWDFUND Act other than the section giving the law its “short title” mandates SEC action. See §§ 302–305.

18 See NEISS ET AL., *supra* note 4, at 37–38; Sherwood Neiss et al., *How 3 Guys Legalized Crowdfunding in 460 Days*, STARTUP EXEMPTION (May 21, 2012), <http://www.startupexemption.com/archives/300>.

19 §§ 302(c), 303(b), 304(a)(2) (calling for SEC rulemaking to be completed by “270 days after the date of enactment of this Act”).

20 See, e.g., Chance Barnett, *Will the S.E.C. Kill Crowdfunding?*, FORBES (Feb. 19, 2013, 1:17 PM), <http://www.forbes.com/sites/chancebarnett/2013/02/19/will-the-s-e-c-kill-crowdfunding/>; Scott Peterson, *Equity Crowdfunding: Will the SEC and FINRA Kill It in its Cradle?*, RELAY STATION SOCIAL MEDIA (Dec. 13, 2012), <http://www.relaystationmedia.com/2012/12/equitycrowdfunding-investments-will-the-sec-and-finra-kill-it-in-its-cradle/>.

21 See Rutheford B Campbell, Jr., *The New Regulation of Small Business Capital Formation: The Impact—If Any—Of the JOBS Act*, 102 KY. L.J. 815, 832 (2014) (“It was . . . clear from the beginning that the mandatory provisions of the Act itself may make it difficult for the Commission to construct an efficient regulatory crowdfunding regime for small businesses in search of external capital.”); Christine Hurt, *Pricing Disintermediation: Crowdfunding and Online Auction IPOs* 37 (March 7, 2014) (Illinois Program in Law, Behavior and Social Science Paper No. LBSS14–27), available at <http://ssrn.com/abstract=2406205> (noting the heavy regulatory burdens imposed through the U.S. Congress’s articulation of the crowdfunding registration exemption in the CROWDFUND Act and describing the exemption as “a bucket of cold water on fantasies of a brave, new world of crowdfunding.”).

22 See, e.g., Hurt, *supra* note 21, at 38–39 (“As expected, the regulations did little to alleviate the restrictions of the CROWDFUND Act, though the SEC was pressured to do so by many commentators. The end result is that the regulations do very little to alter the arguably unworkable regime outlined by Congress.”); William Carleton, *The JOBS Act: Three Things Broken in Investment Crowdfunding That*

Interestingly, however, the SEC—not Congress—frequently is blamed for the defects in the CROWDFUND Act, for which it bears no responsibility.²³ In order to remedy this cost–benefit imbalance, the SEC would have to effectively unravel the work of Congress, a task that it is unlikely to take on.²⁴

So much promise; but so little hope that it has been or will be realized. This statement of regret, which follows logically from the brief history of the

SEC Regulations Won't Fix, VC EXPERTS, https://vcexperts.com/buzz_articles/1305 (last visited Apr. 6, 2014) (arguing that there are three fundamental problems with the JOBS Act that cannot be corrected by SEC regulation); Alexander Davie, *In Spite of What You May Have Heard, the Senate Just Effectively Killed Crowdfunding*, STRICTLY BUS. L. BLOG (Mar. 25, 2012), <http://www.strictlybusinesslawblog.com/2012/03/25/in-spite-of-what-you-may-have-heard-the-senate-just-effectively-killed-crowd-crowdfunding/> (identifying specific amendments added by the Senate to the JOBS Act that will prevent effective crowdfunding); AnnMarie McIlwain & Donald Murray, *Is Crowdfunding to Be Crowdless?*, THE HILL (May 13, 2013, 8:30 PM), <http://thehill.com/blogs/congress-blog/economy-a-budget/299341-is-crowdfunding-to-be-crowdless> (arguing that the high costs of crowdfunding under the JOBS Act will be prohibitive); Charles Wilbanks, *For Crowdfunding, the Revolution Will Be Localized*, CBS NEWS (July 12, 2013, 4:35 PM), <http://www.cbsnews.com/news/for-crowdfunding-the-revolution-will-be-localized/> (quoting this author and identifying hurdles created by the JOBS Act for entrepreneurs engaging in crowdfunding).

23 For example, the title of a recent web blog post attributes the cost of investment crowdfunding to the SEC's rules (although the article itself merely cites to the cost–benefit analysis in the SEC proposal release). Sherwood Neiss, *It Might Cost You \$39K to Crowdfund \$100K Under the SEC's New Rules*, VENTUREBEAT (Jan. 2, 2014, 2:14 PM), <http://venturebeat.com/2014/01/02/it-might-cost-you-39k-to-crowdfund-100k-under-the-secs-new-rules/>. A Twitter user linked to the article in a tweet that read “The SEC is about to ruin crowdfunding.” Radley Balko, TWITTER (Jan. 3, 2014, 8:12 AM), <https://twitter.com/radleybalko/status/419139194326224896>. But others, including members of Congress, also seem confused about the origins of the various restrictions on participants and offerings included in the CROWDFUND Act (at least if one believes journalist and industry reports). See, e.g., Ted Knutson, *Crowd-funding Poses 'Significant Liability' for FAs, Expert Warns*, FIN. ADVISOR (Jan. 16, 2014), <http://www.fa-mag.com/news/crowd-funding-poses-significant-liability-for-fas-expert-warns-16650.html> (citing to and quoting from comments made regarding the SEC rule making by a member of the House of Representatives).

24 See Hurt, *supra* note 21, at 37 (“The statute did leave some of the details to the SEC to flesh out in regulations; however, the SEC could only tighten the detailed statute with more requirements, not fewer.”); *id.* at 38 (“Because Congress made the CROWDFUND Act so detailed, the SEC had very little leeway to subtract, and not much to add, to flesh out the new provisions in the Securities Act.”). Congress has afforded the SEC relatively broad rulemaking authority under the federal securities laws. See Securities Act of 1933, 15 U.S.C. §§ 775, 78mm (2012). Yet, even if this authority could be used to contravene the requirements imposed by Congress in the CROWDFUND Act (which is uncertain, at best), the SEC would not likely use its authority to overwrite congressional actions in the current political and fiscal environment, especially because these congressional undertakings resulted in over ten years of heavy burdens on rulemaking and underfunding. See, e.g., Joan MacLeod Heminway, *Sustaining Reform Efforts at the SEC: A Progress Report*, 30 BANKING & FIN. SERVICES POL’Y REP. 1, 11–12 (Apr. 2011) (noting friction between Congress and the SEC regarding funding); William Alden, *For 2 Wall Street Regulators, More Belt–Tightening*, N.Y. TIMES DEALBOOK (Jan. 14, 2014, 5:13 PM), <http://dealbook.nytimes.com/2014/01/14/for-2-wall-street-regulators-more-belt-tightening/> (describing Congress’ proposed budget cuts for the SEC); Timothy Spangler, *SEC to Congress: “Show Us the Money”*, FORBES (Jan. 23, 2011, 6:41 PM), <http://www.forbes.com/sites/timothyspangler/2011/01/23/sec-to-congress-show-us-the-money/> (illustrating Congress’ limitations on funding for the SEC).

investment crowdfunding movement, captures a dominant theme in the current investment crowdfunding narrative among a growing group of commentators. The democratization of capital formation promised by the CROWDFUND Act is highly improbable regardless of the nature and extent of final rulemaking by the SEC and the Financial Industry Regulatory Authority (“FINRA”). This Article, which builds on earlier work by Professors C. Steven Bradford²⁵ and Stuart Cohn,²⁶ explains the history and current status of the regulation of crowdfunding under the 1933 Act, identifies and describes reasons for despair about the current regulatory environment, and suggests a way forward. The way forward assumes, without further analysis, that the CROWDFUND Act demonstrates the inevitability—even if not the desirability—of a viable 1933 Act registration exemption for crowdfunding.

I. HOW WE GOT TO WHERE WE ARE

The story of investment crowdfunding over the past few years is a classic regulatory tale. It includes economic elements and political elements. Truly, it is a story of political economy, broadly writ. This Part unpacks this history to enable a better understanding of where investment crowdfunding has been, is, and may be.

A. How Is Investment Crowdfunding Regulated Under the CROWDFUND Act?

The CROWDFUND Act amends both the 1933 Act and the Securities Exchange Act of 1934, as amended (“1934 Act”). Among other things, the CROWDFUND Act permits unregistered public offers and sales of securities made under specified conditions by creating a new exemption from 1933 Act registration (the “crowdfunding exemption”).²⁷ Further, the CROWDFUND Act excludes investors purchasing securities in an offering that qualifies for the crowdfunding exemption from the calculation of equity holders for purposes of determining the applicability of the registration requirements of the 1934 Act.²⁸ Although Congress employed traditional tools of securities regulation in composing the CROWDFUND Act (i.e., mandatory disclosure rules, antifraud and other liability provisions, and substantive regulation of participants and conduct), the legislative process was

²⁵ See C. Steven Bradford, *The New Federal Crowdfunding Exemption: Promise Unfulfilled*, 40 SEC. REG. L.J. 195 (2012).

²⁶ See Stuart R. Cohn, *The New Crowdfunding Registration Exemption: Good Idea, Bad Execution*, 64 FLA. L. REV. 1433 (2012), available at <http://scholarship.law.ufl.edu/cgi/viewcontent.cgi?article=1032&context=flr>.

²⁷ JOBS Act, Pub. L. No. 112-106, § 302(a), 126 Stat. 306, 315 (codified at 15 U.S.C. § 77d(a)(6) (2012)).

²⁸ *Id.* § 303(a) (codified at 15 U.S.C. § 78l(g)(6)).

politically driven and not well considered, resulting in a veritable “piling on” of costly investor protection devices and market integrity safeguards.²⁹ As a result, the provisions of the CROWDFUND Act represent a bit of a hodgepodge—a messy accumulation of enabling and protective provisions.

This Article focuses specifically on these provisions—the 1933 Act crowdfunding exemption and related legislative enactments in the 1933 Act and the 1934 Act. The CROWDFUND Act’s new registration exemption for crowdfunded offerings is codified in Section 4(a)(6) of the 1933 Act.³⁰ The exemption is for primary offerings only—offerings by an issuer of securities to investors. To comply with the exemption, an offering must meet a number of requirements.

Specifically, to be exempt from registration under the CROWDFUND Act, both the offering of securities and the purchases made by investors in that offering are limited in dollar amount. Under Section 4(a)(6), issuers may sell no more than \$1,000,000 in any twelve-month period in reliance on the crowdfunding exemption.³¹ In addition, those purchasing securities in offerings under the crowdfunding exemption are limited in the amount they can invest in any twelve-month period to:

(i) the greater of \$2,000 or 5 percent of the annual income or net worth of such investor, as applicable, if either the annual income or the net worth of the investor is less than \$100,000; and

(ii) 10 percent of the annual income or net worth of such investor, as applicable, not to exceed a maximum aggregate amount sold of \$100,000, if either the annual income or net worth of the investor is equal to or more than \$100,000³²

Accordingly, CROWDFUND Act offerings are likely to be conducted by small businesses or for small projects and may involve many purchasers making small dollar-value investments.

The CROWDFUND also regulates the process of conducting an exempt crowdfunded securities offering. Specifically, all CROWDFUND Act offerings must be conducted through a registered intermediary—either a broker (a pre-existing transactional intermediary recognized and regulated under federal and state securities law) or a funding portal (a new transactional intermediary created by the CROWDFUND Act).³³ This intermediation

29 See, e.g., John Wasik, *Crowdfunding Rules: Hurry Up and Wait*, FORBES (June 27, 2012, 3:31 PM), <http://www.forbes.com/sites/johnwasik/2012/06/27/crowdfunding-not-kosher-yet/> (“[C]autious senators injected more investor protection language in the final version of the legislation that could make rulemaking nettlesome.”).

30 Securities Act of 1933, 15 U.S.C. § 77d(a)(6) (2012).

31 *Id.* § 77d(a)(6)(A).

32 *Id.* § 77d(a)(6)(B) (leaving unclear the investment cap if, for example, an investor’s annual income is below the threshold amount and net worth is above the threshold amount).

33 *Id.* § 77d(a)(6)(C); see also Cohn, *supra* note 26, at 1439–40.

requirement, like the per-investor cap, was introduced to the legislation as an investor protection element.³⁴

Issuers desiring to avail themselves of the crowdfunding registration exemption in the CROWDFUND Act must comply with a list of requirements that includes mandatory disclosures (defined in the statute by reference to eight broad subject-matter categories), limitations on advertising and promoter compensation, and periodic reporting.³⁵ The SEC may add to this list of mandates.³⁶ It has taken advantage of this invitation (and expressly indicates that it is doing so) in a number of areas in its proposal release.³⁷ Even without SEC enhancement, however, Congress's articulation of disclosure requirements as set forth in the CROWDFUND Act is relatively precise in certain respects, explicitly calling for the issuer to "file with the Commission and provide to investors and the relevant broker or funding portal, and make available to potential investors" specific information about the issuer, its business operations, its management and security holders, its financial affairs, and its capital structure, and information about the offering and the use of the offering proceeds.³⁸ The specific legislatively mandated disclosures on financial matters include, for example, making available "financial statements reviewed by a public accountant who is independent of the issuer, using professional standards and procedures for such review or standards and procedures established by the Commission, by rule, for such purpose" for offerings over \$100,000 but not over \$500,000 in aggregate amount³⁹ and audited financial statements for offerings over \$500,000 up to the \$1,000,000 cap.⁴⁰

Each broker or funding portal acting as an intermediary under the CROWDFUND Act also must comply with certain requirements in order for an offering to qualify for the crowdfunding exemption.⁴¹ For example, the statute requires an intermediary to register with the SEC and the applicable

34 See Cohn, *supra* note 26, at 1439 (2013).

35 15 U.S.C. § 77d-1(b)(1)-(4) (2012); see also Bradford, *supra* note 25, at 202-05; Cohn, *supra* note 26, at 1441-43.

36 15 U.S.C. § 77d-1(b)(5); see also Campbell, *supra* note 21.

37 See, e.g., Crowdfunding, Securities Act Release No. 9470, Exchange Act Release No. 70741, 78 Fed. Reg. 66,428, at 173, 391 (requiring an intermediary to provide investor-to-investor and investor-to-issuer communication channels on its platform, subject to certain conditions) (proposed Oct. 23, 2013), available at <http://www.sec.gov/rules/proposed/2013/33-9470.pdf>; see also Campbell, *supra* note 21, at 833-36 (noting and criticizing mandatory disclosure provisions required by the SEC). These augmentations appear to be driven, at least to some extent, by common sense or other mandates within and features of the CROWDFUND Act (including, e.g., risk reduction requirements imposed on intermediaries and the misstatements and omissions liability imposed on principals of the business). See *infra* note 68 and accompanying text.

38 *Id.* § 77d-1(b)(1).

39 *Id.* § 77d-1(b)(1)(D)(ii).

40 *Id.* § 77d-1(b)(1)(D)(iii).

41 See generally Cohn, *supra* note 26, at 1440-41 (describing the requirements and obligations of intermediaries under the CROWDFUND Act).

self-regulatory organization (i.e., FINRA), and to make certain disclosures of its own (including disclosures of risk-related and investor education information).⁴² Funding portals are subject to additional strictures.⁴³ Specifically, they cannot “offer investment advice or recommendations,”⁴⁴ “solicit purchases, sales, or offers to buy the securities offered or displayed on its website or portal,”⁴⁵ “compensate employees, agents, or other persons for such solicitation or based on the sale of securities displayed or referenced on its website or portal,”⁴⁶ “hold, manage, possess, or otherwise handle investor funds or securities,”⁴⁷ or “engage in such other activities as the Commission, by rule, determines appropriate.”⁴⁸ The CROWDFUND Act also makes all brokers and finding portals acting as crowdfunding intermediaries responsible for a variety of tasks, including (among others):

- guaranteeing that each investor “reviews investor-education information;”⁴⁹
- affirming each investor’s understanding that he, she, or it “is risking the loss of the entire investment, and that the investor could bear such a loss;”⁵⁰
- ensuring that each investor answers questions demonstrating—
 - (i) “an understanding of the level of risk generally applicable to investments in startups, emerging businesses, and small issuers;”⁵¹
 - (ii) “an understanding of the risk of illiquidity; and”⁵²
 - (iii) “an understanding of such other matters as the Commission determines appropriate, by rule;”⁵³

⁴² 15 U.S.C. § 77d-1(a)(1)-(3).

⁴³ See generally Bradford, *supra* note 25, at 220-22 (summarizing and critiquing restrictions on funding portals).

⁴⁴ 15 U.S.C. § 78c(a)(80)(A) (2012).

⁴⁵ *Id.* § 78c(a)(80)(B).

⁴⁶ *Id.* § 78c(a)(80)(C).

⁴⁷ *Id.* § 78c(a)(80)(D).

⁴⁸ *Id.* § 78c(a)(80)(E).

⁴⁹ 15 U.S.C. § 77d-1(a)(4)(A) (2012).

⁵⁰ *Id.* § 77d-1(a)(4)(B).

⁵¹ *Id.* § 77d-1(a)(4)(C)(i).

⁵² *Id.* § 77d-1(a)(4)(C)(ii).

⁵³ *Id.* § 77d-1(a)(4)(C)(iii).

- taking fraud risk reduction measures, “including obtaining a background and securities enforcement regulatory history check on each officer, director, and person holding more than 20 percent of the outstanding equity of every issuer whose securities are offered by such person;”⁵⁴
- affording the SEC and potential investors access, within 21 days after “the first day on which securities are sold to an investor,” to information provided by the issuer under the provisions of the CROWDFUND Act described above;⁵⁵
- overseeing the retention and distribution of the offering proceeds to ensure that they are not released to the issuer until “the aggregate capital raised from all investors” satisfies the target offering amount established by the issuer, and allowing investors to withdraw their commitments to invest;⁵⁶
- acting to ensure compliance with the twelve-month investment limits for issuers described above;⁵⁷
- helping to protect the privacy of investor information;⁵⁸
- not compensating “promoters, finders, or lead generators for providing the broker or funding portal with the personal identifying information of any potential investor”;⁵⁹
- prohibiting its management from having a financial interest in an issuer that has retained its services;⁶⁰ and
- complying with other requirements prescribed by the SEC.⁶¹

Congress supported these offering requirements for issuers and intermediaries with a new misstatements and omissions liability provision

⁵⁴ *Id.* § 77d–1(a)(5).

⁵⁵ *Id.* § 77d–1(a)(6).

⁵⁶ *Id.* § 77d–1(a)(7).

⁵⁷ *Id.* § 77d–1(a)(8).

⁵⁸ *Id.* § 77d–1(a)(9).

⁵⁹ *Id.* § 77d–1(a)(10).

⁶⁰ *Id.* § 77d–1(a)(11).

⁶¹ *Id.* § 77d–1(a)(12). In fact, many of the other requirements imposed on issuers and intermediaries under the CROWDFUND Act also are expressly qualified because the Act specifically designates the SEC’s ability or obligation to make further provisions. *See, e.g., id.* § 77d–1(a)(3)–(9), (b)(1)(I), (b)(3)–(4).

modeled on and, in the crowd-funded offering context, analogous to the pre-existing misstatements and omissions liability provision found in Section 12(a)(2) of the 1933 Act.⁶² Under this new liability provision, a purchaser of securities in an offering subject to the crowdfunding exemption may bring a legal action against the issuer of the offered securities for any written or oral communication made by the issuer that includes an untrue statement of material fact or omits to state a material fact necessary to make statements made in the communication not misleading.⁶³ The purchaser may not recover if he, she, or it knew of the untruth or omission.⁶⁴ An issuer has the burden of proving it “did not know, and in the exercise of reasonable care could not have known, of such untruth or omission.”⁶⁵

In October 2013, the SEC released its proposed rules under the CROWDFUND Act.⁶⁶ Some public commentators cried out “Hallelujah!” and expressed the view that investment crowdfunding was finally on its way to becoming a reality.⁶⁷ Most were more subdued in their responses, and an increasing number of commentators began to acknowledge that the SEC had principally followed Congress’s directives in its rulemaking and, for the most part, declined Congress’s invitation to add significant burdens to those already created under the CROWDFUND Act.⁶⁸ One observer poignantly offered: “There’s nothing the SEC can do to make non-accredited crowdfunding under Title III of the JOBS Act cost-efficient. The essential problem is that Congress wrote a mini-registration law, rather than authorizing the agency to craft a crowdfunding exemption.”⁶⁹ However, many overtly or implicitly blamed the

62 Securities Act of 1933, 15 U.S.C. § 77f(a)(2) (2012).

63 See § 77d-1(c)(1)-(2)(A).

64 *Id.* § 77d-1(c)(2)(A).

65 *Id.* § 77d-1(c)(2)(B).

66 Crowdfunding, Securities Act Release No. 9470, Exchange Act Release No. 70741, 78 Fed. Reg. 66,428 (proposed Oct. 23, 2013), available at <http://www.sec.gov/rules/proposed/2013/33-9470.pdf>.

67 See, e.g., Devin Thorpe, *Where Does Crowdfunding Go from Here? Experts Explain*, FORBES (Feb. 1, 2014, 7:37 PM), <http://www.forbes.com/sites/devinthorpe/2014/02/01/where-does-crowdfunding-go-from-here-experts-explain/> (“Crowdfunding is going mainstream.”).

68 See, e.g., Ashley Adelman, *SEC’s Crowdfunding Rules Open for Public Comment*, ACCESS TO CAPITAL (Dec. 11, 2013), <http://accesstocapital.com/secs-crowdfunding-rules-open-for-public-comment/> (noting that “the proposed rules are almost identical to the JOBS Act”); Gabrielle Karol, *SEC’s New Crowdfunding Rules Explained*, FOX SMALL BUSINESS CENTER (Oct. 24, 2013), <http://smallbusiness.foxbusiness.com/finance-accounting/2013/10/24/sec-new-crowdfunding-rules-explained/> (“McDermott, Will & Emery partner Thomas Murphy, who heads up the firm’s securities and capital markets group, says the SEC more or less stuck to the letter of the law.”); Brian Korn, *SEC Proposes Crowdfunding Rules*, FORBES (Oct. 23, 2013, 2:41 PM), <http://www.forbes.com/sites/deborahljacobs/2013/10/23/sec-proposes-crowdfunding-rules/> (“[T]he SEC’s hands are tied since the JOBS Act itself creates most of the restrictions in the proposed rule.”).

69 William Carleton, *The Fault Lies Not in Our Agencies, but in Our Congresses*, WILLIAM CARLETON, COUNS. @ L. (Jan. 22, 2014), <http://www.wac6.com/wac6/2014/01/the-fault-lies-not-in-our-agencies-but-in-our-congresses.html>; see also Hurt, *supra* note 21, at 37 (“Many

SEC for effectively nullifying the great promise of investment crowdfunding through over-regulation or for under-regulating to achieve investor-protection and market-integrity objectives.⁷⁰

The proposed SEC rules are collected under “Regulation Crowdfunding,” a new body of rules under the 1933 Act and the 1934 Act.⁷¹ The SEC’s rulemaking proposal is 585 pages long and, in most respects, implements and adds essential or anticipated details to Congress’s mandates in the CROWDFUND Act.⁷² In fact, the SEC posits almost 300 numbered questions on which it is requesting comments (in addition to requesting general comments and comments on its economic analysis), many of which ask about the need for or desirability of requirements in excess of what Congress provided.⁷³ As earlier noted, there are areas in which the SEC adds to the congressional framework provided in the CROWDFUND Act,⁷⁴ but these enhanced protections for investors and markets are expressly noted and add minimal heft to Congress’s already weighty exemption requirements.

B. What Contributed to the Current Investment Crowdfunding Regulatory Scheme?

As I think about the CROWDFUND Act and the SEC rulemaking under it in the context of the greater crowdfunding phenomenon, I am constantly reminded of the following infamous line in the Talking Heads song, *Once in a Lifetime*: “[Y]ou may ask yourself—well... How did I get here?”⁷⁵ The process has a bit of an existential feel to it, just like the song. Over a five-year period, crowdfunding—including some investment crowdfunding—grew from individual experiments in web-based business finance to a veritable international movement with, as is so often the case, regulators playing catch-up with the market.

commentators who were hoping for an exemption that would provide a cheap and easy path to crowdfunding bemoaned the cost of disclosure, particularly ongoing disclosure, as well as other costly requirements.”).

70 See, e.g., Campbell, *supra* note 21, at 833 (“Setting the efficient level of mandatory disclosure is certainly the most difficult decision for the Commission in connection with its regulatory implementation of the Crowdfunding Act, and I fear the Commission has missed it badly in this first iteration.”); Gene Marks, *Seriously Ridiculous: Rethinking the SEC’s Proposed Crowdfunding Rules*, Inc., <http://www.inc.com/gene-marks/rethinking-sec-proposed-crowdfunding-rules.html> (last updated Nov. 7, 2013) (“[T]he SEC proposal is drawing some well-deserved criticism.”).

71 Crowdfunding, Securities Act Release No. 9470, Exchange Act Release No. 70741, 78 Fed. Reg. 66,428 (proposed Oct. 23, 2013), available at <http://www.sec.gov/rules/proposed/2013/33-9470.pdf>.

72 See *id.*

73 See *id.*

74 See, e.g., *id.* at 36 (describing ways in which the proposed rules add categories of issuers excluded from exemption eligibility).

75 TALKING HEADS, *Once in a Lifetime*, on REMAIN IN LIGHT (Sire Records 1980).

I first became aware of and began to follow crowdfunding in or about 2007, when National Public Radio aired a segment on crowdfunded music albums, which featured early crowdfunding sites SellaBand and Slicethepie.⁷⁶ My husband alerted me to the segment, noting that it seemed like the kind of business model I would care about because it sounded like it could involve a sale of securities. He was right. I immediately began looking into the business model (then operating in Europe), and I found it provided great illustrations for the investment contract section of the “What is a security?” part of my Securities Regulation course. I used SellaBand and Slicethepie (with some altered facts connecting their business to the U.S.) on my final exam for Securities Regulation in the spring of 2008. Since that time, crowdfunding has been a topic covered on either my midterm or final exam for that course.

In January 2010, I received an email message from someone who had found an online video of a lecture that I gave describing my 2009 midterm exam in Securities Regulation (my first experiment with an oral midterm exam). My email correspondent, Josh, was an entrepreneur with a law degree and international experience in small business finance. He was interested in starting up a website to crowdfund social enterprises. The catch? He wanted to be able to offer funders a small profit-sharing or revenue-sharing increment. He eventually did found, operate, and unwind that crowdfunding business, which was featured in my original, coauthored article on crowdfunding.⁷⁷ Over the many months that Josh and I communicated (mostly through email), Josh suggested a number of times that I speak and write on the topic, since no one else who he had contacted both understood the business model and had taken an interest in the legal aspects of the business model. This interchange encouraged my continuing research on crowdfunding (crowdfund investing in particular), eventually led to my written work in this area, and frames my view of investment crowdfunding and the CROWDFUND Act.

What I learned from Josh and from my research built on my general legal, academic, and practical knowledge of corporate finance and securities regulation. There was (and is) a significant funding gap for small private business ventures—especially startups—that is not being filled by friends-and-family, seed, angel, and venture capital.⁷⁸ There also was (and is)

⁷⁶ See generally Eliot Van Buskirk, *Put Your Money Where Your Indie Rock Is*, WIRED (Mar. 3, 2008), http://www.wired.com/entertainment/music/commentary/listeningpost/2008/03/listeningpost_0303 (describing how music fans have turned into music investors through crowdfunding on SellaBand and Slicethepie).

⁷⁷ See Heminway & Hoffman, *supra* note 5, at 892 n.60 and accompanying text.

⁷⁸ See generally Darian M. Ibrahim, *The (Not So) Puzzling Behavior of Angel Investors*, 61 VAND. L. REV. 1405, 1416–18 (2008) (describing this funding gap); Thomas G. James, *Far from the Maddening Crowd: Does the JOBS Act Provide Meaningful Redress to Small Investors for Securities Fraud in Connection with Crowdfunding Offerings?*, 54 B.C. L. REV. 1767, 1771–72 (2013) (same); Knight et al., *supra* note 8, at 139 (noting that “[t]he company that needs just a few hundred thousand dollars has faced a considerable challenge.”); David Mashburn, Comment, *The Anti-Crowd Pleaser: Fixing the Crowdfund Act’s Hidden Risks and Inadequate Remedies*, 63 EMORY L.J. 127,

some frustration among members of the general public, most of whom are typically shut out of investing in early-stage ventures under traditional means of financing small businesses.⁷⁹ Crowdfunding, Internet offerings to an unlimited audience (as originally conceived and organically grown), strives to meet both needs—those of small business entrepreneurs and those of the general public investment community—by offering funding opportunities for businesses or projects over the Internet without regard to the investor’s geographic location, net worth, annual salary, or pre-existing relationship to the entrepreneurs, their business, or their project.

Early investment crowdfunding initiatives, unregistered (and therefore illegal) as they were and are, are part of the fabric of crowdfunding as it has begun to develop. Histories of the crowdfunding movement and investment crowdfunding are related in varying degrees of detail and with varying areas of emphasis.⁸⁰ Many, if not most, of these histories, however, ignore the reality that various crowdfunding websites have been offering and selling investment interests that are securities without registering those offerings under the 1933 Act. ProFounder, which ceased operations in early 2012, is the most widely publicized example of this reality,⁸¹ but other similar websites have existed and continue to exist.⁸²

This unique part of the history of investment crowdfunding—the natural emergence of a new market for securities offerings—flies under the radar for many observers. Why? Because those observers typically do not recognize that the interests in businesses and projects offered through these crowdfunding websites are, in fact, securities. That lack of recognition likely results from the fact that the websites were not offering equity (stock) or debt instruments (debentures or notes). Instead, they were offering what securities lawyers know as “investment contracts.” An investment contract is “a contract, transaction or

139–43 (2013) (same); Jeffrey E. Sohl, *The U.S. Angel and Venture Capital Market: Recent Trends and Developments*, 6 J. PRIVATE EQUITY 7, 14 (2003) (same).

79 See Knight et al., *supra* note 8, at 139 (noting that “the ability of a person of average means to participate as an investor in the start-up world has been almost nonexistent.”). For example, because these investors often are neither accredited investors as defined in Regulation D, see 17 C.F.R. § 230.501 (2014), nor sophisticated for purposes of offerings conducted Rule 506 under Regulation D, see 17 C.F.R. § 230.506(b)(2)(ii), they are not often solicited to participate in Regulation D offerings.

80 See, e.g., KEVIN LAWTON & DAN MAROM, *THE CROWDFUNDING REVOLUTION* 47–66 (2013); NEISS ET AL., *supra* note 4, at 23–40; YOUNG, *supra* note 4, at 55–56.

81 See Amy Cortese, *The Future of Crowdfunding*, LOCAVESTING (Feb. 23, 2012), <http://locavesting.blogspot.com/2012/02/future-of-crowdfunding.html>; Leena Rao, *Fundraising Platform for Startups ProFounder Shuts Its Doors*, TECHCRUNCH (Feb. 17, 2012), <http://techcrunch.com/2012/02/17/startup-fundraising-platform-profounder-shuts-its-doors/>.

82 My original coauthored crowdfunding article featured one of these firms, 33needs, which also ceased operations before passage of the CROWDFUND Act. See Heminway & Hoffman, *supra* note 5, at 892 n.60 and accompanying text; see also Anthony Ha, *33needs Helps Do-Gooder Startups Crowdfund Their Funding*, VENTUREBEAT (Jan. 31, 2011, 9:01 PM), <http://venturebeat.com/2011/01/31/33needs-launch/>; Tristan Pollock, *33Needs Turning Ideas into Action*, NEXT BILLION (Jan. 21, 2011), <http://nextbillion.net/33needs>.

scheme whereby a person invests his money in a common enterprise and is led to expect profits solely from the efforts of a promoter or a third party.”⁸³

Specifically, these crowdfunding websites were offering investment contracts that I have come to call “unequity:” “a particular type of financial interest that provides for profit-sharing or revenue-sharing on a short-term basis, with no accompanying governance rights.”⁸⁴ For example, a fashion designer might solicit funds from the crowd in \$10 increments to help finance her first collection and promise funders a share of her profits from the resulting sales of that collection proportional to the amount of each funder’s contribution. Or a software application developer might ask the crowd for financial backing and agree to give investors a fraction of the sales price of one or more copies of the application in exchange for a particular amount invested. Unlike common equity investors, these funders have no ability to choose the management of the venture or define or change the business or operations of the venture funded; unlike convertible preferred equity investors, these funders have no ability to acquire an equity interest in the business or project; and, unlike redeemable preferred equity and debt investors, these funders do not have a right to repayment of the principal amount invested.

In fact, the typical unequity offering is not intended to (and may not) result in pecuniary gain to the investor. Rather, the gain comes in part from financial return and in part from other return, often in the form of a tangible reward (i.e., a good or service) or altruism (e.g., for social enterprise investments or for funding the little guy with the creative idea who otherwise would not be able to execute on his idea), happiness or pride (e.g., by developing a two-way relationship with an entrepreneur—being able to say that you contributed to and received proceeds from a startup’s business), or other emotional satisfaction. Typically, the promoters of the businesses and projects seeking funding through unequity are looking for small amounts of investment capital from their crowdfunded offerings—closer to the amounts typically sought on donation and reward crowdfunding websites like Kickstarter and Indiegogo than to the amounts typically raised by equity crowdfunding websites in other countries.⁸⁵

The CROWDFUND Act does not efficiently foster this organically grown market for capital, which had promise to well serve startups in certain lines of

83 SEC v. W.J. Howey Co., 328 U.S. 293, 298–99 (1946).

84 Joan MacLeod Heminway, *What Is a Security in the Crowdfunding Era?*, 7 OHIO ST. ENTREPREN. BUS. L.J. 335, 360–61 (2012); see also Joan MacLeod Heminway, *To Be or Not to Be (a Security): Funding For-Profit Social Enterprises*, 25 REGENT U. L. REV. 299, 312 n.50 (2013).

85 See CROWDSOURCING, LLC., CROWDFUNDING INDUSTRY REPORT: MARKET TRENDS, COMPOSITION AND CROWDFUNDING PLATFORMS (ABRIDGED VERSION) (May 2012), available at <http://www.crowdfunding.nl/wp-content/uploads/2012/05/92834651-Massolution-abridged-Crowd-Funding-Industry-Reporttr.pdf> (showing that most crowdfunded equity offerings raise \$50,001–\$100,000 and most donation-based or rewards-based crowdfunded offerings raise less than \$2500); see also *Kickstarter Stats*, KICKSTARTER, (last visited Apr. 6, 2014), <https://www.kickstarter.com/help/stats> (“Most successfully funded projects raise less than \$10,000, but a growing number have reached six and even seven figures.”).

business. Enthusiasm and the desire to offer broad-based support for small business likely drove the inclusion of \$1,000,000 cap in the CROWDFUND Act.⁸⁶ Given that crowdfunded offerings were being made at that level (although not many), it might have seemed to congressional sponsors that a \$1,000,000 cap was reasonable. Setting the cap at \$1,000,000 also put the crowdfunding registration exemption in the same, relatively unregulated environment in which the limited offering registration exemption provided for in Rule 504 of Regulation D under the 1933 Act⁸⁷ operates. To many of us watching the crowdfunding sector, however, \$1,000,000 seemed like a high maximum aggregate offering amount to permit, given that investment crowdfunding represents a relatively untested offering method and segment of the capital markets.⁸⁸ The fear that non-accredited investors would desire to invest significant amounts of money in an offering of this size drove the inclusion of sundry investor protection provisions in the CROWDFUND Act: the individual investment limits, detailed statutorily ordained mandatory disclosures, the requirement that offerings be conducted through a broker or funding portal (and the obligations and restrictions imposed on broker and funding portal activities), and the new misstatements liability scheme.⁸⁹

Given presidential support and bipartisan backing in Congress (after all, who wants to oppose a bill that effectively promises to increase and broaden the base of investment capital and, perhaps, spur entrepreneurial activity and job creation during an economic downturn?),⁹⁰ there undeniably was significant political pressure to pass the CROWDFUND Act. This environment fostered rushed congressional decisions on the aggregate offering limit and, flowing from that, hurried, compromise-driven determinations to add significant burdens on issuers, intermediaries, and investors to the crowdfunding

86 In fact, the earliest version of the bill that eventually became the CROWDFUND Act included a cap. See *Entrepreneur Access to Capital Act*, H.R. 2930, 112th Cong. § 2(a) (2011).

87 17 C.F.R. § 230.504 (2014).

88 *E.g.*, Cohn, *supra* note 26, at 1437 (noting that “registration exemptions for offerings for not more than \$250,000, or offerings up to \$500,000 with investments limited, for example, to no more than \$1,000, would have addressed many if not most crowdfunding situations”).

89 *See id.* at 1438 (“The problem with having selected one million dollars as the authorized amount is that Congress then felt impelled to surround the exemption with numerous requirements that might not have been necessary had an exemption been created for smaller offerings in lieu of or in addition to the one million dollar exemption.”); Knight et al., *supra* note 8, at 137 (describing the heavy, traditional regulation in the CROWDFUND Act as “less ‘Kickstarter plus’ and more ‘Merrill minus.’”); John S. (Jack) Wroldsen, *The Social Network and the Crowdfund Act: Zuckerberg, Saverin, and Venture Capitalists’ Dilution of the Crowd*, 15 VAND. J. ENT. & TECH. L. 583, 598–99 (2013) (describing the political process behind the inclusion of the referenced investor protection provisions in the CROWDFUND Act); *see also supra* notes 33–65 and accompanying text (describing the referenced investor protection provisions in the CROWDFUND Act).

90 *See supra* notes 11–13; Jeff Howe, *Senators Introduce a Bi-Partisan Crowdfunding Bill*, CROWDSOURCING.ORG (Mar. 13, 2012, 8:57 PM), <http://www.crowdsourcing.org/editorial/senators-introduce-a-bi-partisan-crowdfunding-bill/12311>.

exemption.⁹¹ Unquestionably, Congress's lack of knowledge and experience in securities regulation and corporate finance—as a broadly representative body of individuals with varied backgrounds and loyalties—played a role in the way the political process translated policy and concepts into the text of the final version of the legislation.

No doubt the SEC, as the expert securities regulator in the federal government, would have been better able to make required and desired tradeoffs and create a more nuanced, cost-effective exemption for crowdfunded offerings. Having said that, as many commentators have noted, the SEC struggled with the desirability of introducing a registration exemption for crowdfunding before and during the legislative process.⁹² This hostile dynamic involving the SEC effectively forced proponents of the exemption into Congress's politically charged, compromise-driven, non-expert environment in order to achieve their objectives. The SEC's uneasiness about crowdfunding and its foot-dragging in proposing rules under the CROWDFUND Act also clearly color many observers' reactions to the SEC rulemaking process—making the SEC an easier scapegoat for the actual and anticipated failings of the CROWDFUND Act.⁹³

II. WHY THE CROWDFUND ACT IS SUBOPTIMAL INVESTMENT CROWDFUNDING REGULATION

Why and how does the crowdfunding exemption come up short in achieving its objectives? In one word, the answer is: *costs*. The costs for small business issuers and intermediaries that are built into the CROWDFUND Act

91 See Cohn, *supra* note 26, at 1434 (“Congress’s rush to action resulted in a statute that appears to have failed in its primary purpose to assist entrepreneurs and others seeking to raise small amounts of capital through broad-based solicitation and may have made matters worse through its heavy-handed regulatory action.”). One investment crowdfunding advocate, who participated in the legislative process that resulted in the passage of the CROWDFUND Act, noted the relative speed with which that process moved:

We had been told that, even if we did get a bill submitted, it could take five to ten years for it to move through the House and Senate to final passage and presidential signature Our actual time between the creation of the Startup Exemption Regulatory Framework and the president’s signing of the JOBS Act was 460 days. Although 460 days feels like a lifetime to an entrepreneur, it’s lightning speed in Washington, D.C.

NEISS ET AL., *supra* note 4, at 37.

92 See, e.g., Campbell, *supra* note 21, at 832 (“It was clear from the beginning that any regulatory implementation of the Act by the Commission would be contentious.”); see also Ben Protess, *Regulator Seeks Feedback on JOBS Act*, N.Y. TIMES DEALBOOK (Apr. 11, 2012, 4:16 PM), <http://dealbook.nytimes.com/2012/04/11/regulator-seeks-feedback-on-jobs-act/> (quoting negative comments from then-SEC Chairwoman Mary Schapiro); Scott Shane, *SEC: Don't Make Crowdfunding Useless for Main Street*, BUSINESSWEEK (Feb. 4, 2013), <http://www.businessweek.com/articles/2013-02-04/sec-don-t-make-crowdfunding-useless-for-main-street> (noting that “the SEC came out strongly against the crowdfunding clause in the JOBS Act, even after it was clear that our elected officials were going to make the tool possible”).

93 See, e.g., Shane, *supra* note 92.

business issuers and intermediaries that are built into the CROWDFUND Act simply are too high in comparison to the expected benefits, especially for small aggregate offering amounts. Although exact costs are difficult to benchmark given the untested nature of the investment crowdfunding market,⁹⁴ commentators have made a number of salient general and specific assertions about the nature or amount of the projected costs associated with compliance with the crowdfunding exemption.

For example, Professor Steve Bradford expressed concern about the complexity and expense of both the disclosure and liability provisions in the crowdfunding exemption. He observed that “[t]he issuer disclosure requirements in the new crowdfunding exemption are neither simple nor inexpensive”⁹⁵ and that

[t]he detailed disclosure requirements in the Act, coupled with the new liability section, are a liability trap for unwary, unsophisticated entrepreneurs. Some issuers are bound to bungle the extensive, complicated disclosures required by the exemption. Since the new liability section has no scienter requirement, those issuers will be liable even if their failure to disclose properly was merely negligent, not intentional.⁹⁶

He ultimately criticized Congress for passing “a poorly drafted regulatory bundle of old ideas that is complicated, expensive, and unlikely to have much of an effect on the small business capital gap.”⁹⁷ Similarly, Professor Stuart Cohn observed that:

[i]t is difficult to imagine that for offerings under \$250,000 either issuers or intermediaries would be willing to undertake the time, cost and risk of potential liabilities. The mandated use of intermediaries, the significant role that intermediaries are expected to play, and the mandated disclosures all point to an impracticable exemption for relatively small offerings. . . .

For the entrepreneurs, artists, project managers, and others seeking to raise relatively small amounts, the crowdfunding exemption is of limited utility. Indeed, the new exemption may have made life more difficult for the truly small promotions by creating an exemption that is impracticable but, having been created with much fanfare, cannot be ignored, unlike the pre-existing situation when crowdfunding existed to some extent beneath regulatory concerns.⁹⁸

He concluded that “[t]he new § 4(6) exemption is an opportunity missed.”⁹⁹ Although Professor Rutheford Campbell finds significant fault with the

94 See Crowdfunding, Securities Act Release No. 9470, Exchange Act Release No. 70741, 78 Fed. Reg. 66,428, at 345–46 (proposed Oct. 23, 2013), available at <http://www.sec.gov/rules/proposed/2013/33-9470.pdf>.

95 Bradford, *supra* note 25, at 217.

96 *Id.*

97 *Id.* at 222.

98 Cohn, *supra* note 26, at 1444–45.

99 *Id.* at 1445; see also Hurt, *supra* note 21, at 44 (characterizing the outlook for investor crowdfunding as “doubtful,” noting that “proponents of crowdfunding despair over the costly restrictions imposed on equity crowdfunding and portals.”); *id.* at 58 (“[T]he long overdue exemption for securities registration seems more likely to choke out quality equity crowdfunding

SEC's rule making, he also lays some blame for the overall expense of the CROWDFUND Act's registration exemption on Congress.¹⁰⁰

Industry representatives and legal experts agree with the scholarly commentary, pointing to issuer audit and disclosure costs¹⁰¹ as well as registration and other costs imposed on intermediaries.¹⁰² One commentator flatly stated that, "[c]ompared to other forms of crowdfunding and capital raising, equity crowdfunding for the public has the worst 'bang for your buck' in all of corporate finance."¹⁰³ Similarly, corporate finance practitioner Thomas Murphy, a partner at McDermott, Will & Emery in Chicago, has commented that the crowdfunding exemption "will be one of the most expensive ways to raise money."¹⁰⁴ As a result, he is skeptical "that crowdfunding is going to be an efficient and viable funding mechanism for very many people."¹⁰⁵ Even crowdfunding advocates admit that the cost-benefit assessment may be a deterrent for potential participants or may dictate the way in which they employ the crowdfunding exemption.¹⁰⁶

than support it.").

100 See Campbell, *supra* note 21, at 832 ("It was also clear from the beginning that the mandatory provisions of the Act itself may make it difficult for the Commission to construct an efficient regulatory crowdfunding regime for small businesses in search of external capital.").

101 It is significant to note that the SEC's proposed rule making under the CROWDFUND Act makes some regulatory choices that mitigate these congressionally imposed costs, including (for example) applying the 12-month aggregate offering limit only to offered securities actually sold by the issuer and permitting accounting firms not registered with the Public Company Accounting Oversight Board to perform audits on issuers using the securities crowdfunding exemption. See Crowdfunding, Securities Act Release No. 9470, Exchange Act Release No. 70741, 78 Fed. Reg. 66,428, at 70-71, 77-78 (proposed Oct. 23, 2013), available at <http://www.sec.gov/rules/proposed/2013/33-9470.pdf>.

102 See, e.g., Andrew Ackerman & Angus Loten, *SEC Moves Ahead with 'Crowdfunding' Proposal*, WALL STREET J., <http://online.wsj.com/news/articles/SB10001424052702303615304579153463087785476> (last updated Oct. 23, 2013, 10:35 PM); Korn, *supra* note 68; Dave Michaels, *Crowdfunding for Internet Stock Sales Approved by SEC*, BLOOMBERG (Oct 24, 2013 12:01 AM), <http://www.bloomberg.com/news/2013-10-23/sec-to-vote-on-crowdfunding-plan-as-white-advances-jobs-act-1-.html>.

103 Korn, *supra* note 68.

104 Karol, *supra* note 68.

105 *Id.*

106 See, e.g., Neiss, *supra* note 23; Paul Spinrad, *How the SEC Listened to the Crowd for Crowdfunding Rules*, PBS MEDIASHIFT (Dec. 4, 2013), <http://www.pbs.org/mediashift/2013/12/how-the-sec-listened-to-the-crowd-for-crowdfunding-rules/>. The strategies for use of the exemption may vary from issuer to issuer, but all will involve an assessment of the amount of cost associated with the benefit to be achieved.

If you are looking to raise money via crowdfunding, the moral of the story is, try to raise as close to the next threshold as possible. The thresholds are at \$100,000, \$500,000, and \$1M. So if you need to raise \$60,000 for your business, aim for \$99,000. Not only will you pay less for that money but you will have more of it. Of course, this assumes you will be able to secure \$99,000 from backers. Same holds true for the \$100,000 to \$500,000 levels and over \$500,000 level. While this was not the intent of the legislation (to force companies to seek more capital than they need), it may make sense when trying to decrease the cost of raising that money.

Potential intermediaries also face significant costs, including the cost of registration. These costs have neither been widely described and discussed nor gone unnoticed. For example, a current crowdfunding entrepreneur, Kendall Almerico, is concerned that complexity and costs will dissuade prospective funding portals from entering the market.¹⁰⁷ He estimates that the cost of entry will total “several hundred thousand dollars.”¹⁰⁸ Adding insult to injury, the CROWDFUND Act limits the revenue-generating activities of funding portals by providing that funding portals may not “offer investment advice or recommendations.”¹⁰⁹ Accordingly, to cover their costs, intermediaries may have to be creative about financing their operations—including by generating a high volume of clients by discounting fees charged to initial and early clients as a loss leader.

The SEC’s rulemaking proposal acknowledges that the high cost of capital for small business issuers is foundational to the CROWDFUND Act’s purpose (i.e., that an objective of the CROWDFUND Act is the avoidance of high costs associated with registered offerings) and is a valid source of concern.¹¹⁰ The proposal release is peppered with references to and questions about costs.¹¹¹ The SEC’s economic analysis in the proposal release¹¹² also, by necessity, raises cost issues, and the SEC is honest about their origins: “While the costs and benefits of the proposed rules in large part stem from the statutory mandate of Title III, certain costs and benefits are affected by the discretion we propose to exercise in connection with implementing this mandate.”¹¹³

Ultimately, however, the SEC’s analysis of the costs and benefits of its rulemaking under the crowdfunding exemption, like similar analyses of costs and benefits offered by others (including those noted above), is necessarily conjectural or inconclusive. At the outset of its analysis, the SEC notes that the “costs and benefits are difficult to quantify or estimate with any degree of certainty, especially considering that Section 4(a)(6) provides a new method

Neiss, *supra* note 23.

¹⁰⁷ Karol, *supra* note 68.

¹⁰⁸ *Id.*

¹⁰⁹ See JOBS Act, Pub. L. No. 112–106, § 304(b), 126 Stat. 306, 315 (codified at 15 U.S.C. § 78c(a)(80)(A) (2012)).

¹¹⁰ See Crowdfunding, Securities Act Release No. 9470, Exchange Act Release No. 70741, 78 Fed. Reg. 66,428, at 344 (proposed Oct. 23, 2013), available at <http://www.sec.gov/rules/proposed/2013/33-9470.pdf> (“The crowdfunding provisions of the JOBS Act were designed to help provide startups and small businesses with capital by making relatively low dollar offerings of securities less costly.”); *id.* at 12 (“We are mindful of the costs imposed by, and the benefits to be obtained from, our rules.”).

¹¹¹ See, e.g., *id.* at 46, 71, 78, 80, 85, 86, 94, 105, 106, 144–45, 146, 166, 167, 189, 258, 265, 268, 280.

¹¹² The SEC’s extensive, albeit necessarily incomplete and inexact, cost–benefit analysis in the proposal release is driven by statutory and regulatory mandates as well as judicial review. See, e.g., 15 U.S.C. § 77b(b) (2012); *id.* § 78c(f) & § 78w(a)(2); Business Roundtable v. Sec’s & Exch. Comm’n, 647 F.3d 1144 (D.C. Cir. 2011).

¹¹³ *Id.* at 317.

for raising capital in the United States.”¹¹⁴ Although the SEC has estimated the compliance costs attendant to each aspect of its rulemaking under the CROWDFUND Act,¹¹⁵ the actual costs and realizable benefits of the crowdfunding exemption, as implemented through the SEC’s rulemaking, will depend on the number and nature of the issuers, investors, and intermediaries that participate in investment crowdfunding—which are unknown at the present time.¹¹⁶ Consequently, the SEC’s economic assessments are qualified by use of words like “could,” “might,” and “would.”¹¹⁷

In the absence of data based on a pre-existing investment crowdfunding market, the reactions of potential market participants may best indicate the significance of the costs of compliance with the crowdfunding exemption. Although the CROWDFUND Act seeks to democratize capital creation by expanding the number and type of investors (as one part of the JOBS Act’s more general strategy of increasing capital formation through innovations to public and private offering processes),¹¹⁸ market observers suggest that the costs of participation in the crowdfunding exemption are driving eligible issuers and intermediaries to the less costly, more efficient offering process under Rule 506 of Regulation D found in the 1933 Act.¹¹⁹ The SEC modified Rule 506 in accordance with the mandate provided in Title II of the JOBS Act to allow for general solicitation of and advertising to and for an unlimited number of non-accredited investors, even over the Internet, provided that all sales are made to accredited investors (including, e.g., institutional investors, high net-worth individuals, and others who are considered, under applicable SEC rules in Regulation D, better able to bear the risk of loss of their entire investment).¹²⁰ This change has generated new and additional interest in the use of Rule 506 (which has been the darling of the transactional exemptions

¹¹⁴ *Id.* at 345.

¹¹⁵ *See id.* at 353–421.

¹¹⁶ *See, e.g., id.* at 345–53 (describing the overall economic effects of the crowdfunding exemption).

¹¹⁷ *See id.*

¹¹⁸ The JOBS Act is styled as legislation “[t]o increase American job creation and economic growth by improving access to the public capital markets for emerging growth companies.” JOBS Act, Pub. L. No. 112–106, 126 Stat. 306 (2012) (pmb.); *see* Mark Landler, *Obama Signs Bill to Promote Start-Up Investments*, N.Y. TIMES, Apr. 6, 2012, at A12, available at <http://www.nytimes.com/2012/04/06/us/politics/obama-signs-bill-to-ease-investing-in-start-ups.html> (describing and quoting the President’s remarks on the objectives of the JOBS Act and the CROWDFUND Act at the JOBS Act signing ceremony).

¹¹⁹ 17 C.F.R. § 230.506 (2014); *see* Bradford, *supra* note 25, at 222–23 (noting the advantages of the Rule 506 amendments for issuers desiring to raise capital over the Internet); Hurt, *supra* note 21, at 44 (“[W]ith the lifting of the ban on general solicitation for Rule 506 private placements, issuers may engage in ‘accredited crowdfunding’ without a registered portal, under that exemption and not Section 4(6).”); *id.* at 58 (“[L]iberalization of other registration exemptions will channel quality projects from ‘retail crowdfunding’ under Section 4(6) to ‘accredited crowdfunding’ under Rule 506 of Regulation D.”).

¹²⁰ *See* 17 C.F.R. §§ 230.501, 230.506(b).

from registration under the 1933 Act) among those who might also use the crowdfunding exemption. The SEC acknowledges the possibility that some issuers may be able to avail themselves of other exemptions, including Rule 506 as amended by the JOBS Act.¹²¹ In fact, both issuers and intermediaries may find that a comparative cost–benefit analysis favors the use of Rule 506 over the crowdfunding exemption or may, as one crowdfunding advocate has suggested, determine it beneficial to adopt a strategy of conducting offerings under both exemptions.¹²²

Given the high cost associated with use of the crowdfunding exemption, the increased interest in, and efficacy of, Rule 506 threatens to undercut the ostensible capital–broadening purpose of the CROWDFUND Act. This risk has generated discussion, criticism, and calls for change.

Polymakers should harmonize two sections of the JOBS Act that run the risk of benefitting wealthy investors at the expense of the crowd. One portion of the law permits mass marketing of less regulated private offerings so long as sales are made to verified accredited investors. Another portion creates a detailed framework for crowd investing, but includes a number of built-in registration, education, investment cap, and disclosure requirements.

Because of lower anticipated regulatory burdens and costs, many investment platforms have shifted attention to facilitating capital-raising from accredited investors. It remains unclear to what extent entrepreneurs or investment platforms will ultimately engage the crowd. Polymakers must be careful not to create a two-tiered system whereby the wealthy investors receive the best investment opportunities and the crowd is left with what remains.¹²³

A two-tiered system in which the general public—which includes non-accredited investors—is left with unattractive investment options is inconsistent with the spirit underlying the CROWDFUND Act. If, as I contend, the costs of complying with the crowdfunding exemption shut promising small businesses (both potential issuers and intermediaries) out of the capital market or shift their preferences to private placement transactions involving a limited, elite group of investors, then the CROWDFUND Act will have failed in its mission and constitutes a waste of congressional and SEC resources. Yet, there may be a way to leverage these sunk transaction costs to achieve more of the objectives that motivated Congress’s consideration and adoption of the CROWDFUND Act.

¹²¹ Crowdfunding, Securities Act Release No. 9470, Exchange Act Release No. 70741, 78 Fed. Reg. 66,428, at 345–46 (proposed Oct. 23, 2013), available at <http://www.sec.gov/rules/proposed/2013/33-9470.pdf>.

¹²² See Neiss, *supra* note 23 (proposing a strategy for maximizing aggregate offering amounts and limiting capital raising costs through use of both the crowdfunding exemption and a private placement using general solicitation under Rule 506(c) of the 1933 Act); see also Hurt, *supra* note 21, at 51 (“Commentators predict that accredited crowdfunding under Rule 506 will eclipse retail crowdfunding and make the latter merely a back-up plan for hard-to-fund issuers.”).

¹²³ Daniel Gorfine, *How to Finish What the JOBS Act Has Started*, FORBES (Dec. 4, 2013, 8:45 AM), <http://www.forbes.com/sites/realspin/2013/12/04/how-to-finish-what-the-jobs-act-has-started/>.

III. WHAT WE CAN DO NOW TO RESCUE INVESTMENT CROWDFUNDING

The federal system of securities regulation—a system designed to encourage capital formation through investor protection and market integrity maintenance fashioned by mandatory disclosure, fraud and other liability, and substantive regulation of participants and their conduct—is a puzzle. Solving the puzzle to support and encourage any individual desired securities offering market requires that regulators effectively balance the costs and benefits to the core players in the market—the three I's: issuers, investors, and intermediaries—to best ensure that each is incentivized to participate. The perceived costs of the crowdfunding exemption to issuers and intermediaries are high enough to raise significant concerns among prospective issuers and intermediaries about whether the benefits are sufficient to support their involvement. Benefits and costs to investors may not be perfectly well balanced, but they are less skewed against participation.

The investment crowdfunding disincentives for issuers and investors are particularly strong and apt in the case of low dollar-value offerings (in which the aggregate pecuniary benefits are limited) for small businesses at early stages of development.¹²⁴ This is unfortunate, since small, early-stage businesses conducting limited dollar-value offerings may be most likely to need the new “friends” that crowdfunding could provide.¹²⁵ They have tapped out their friends and family but are not yet (or may never be) ripe for new investor, late-stage seed, angel, or venture capital infusions. This type of entity or business project was the type of issuer that was innovatively using investment crowdfunding before the adoption of the JOBS Act (i.e., until light was cast on the need to register offers and sales of the investment interests being offered).¹²⁶ Although the SEC has expressed doubts that there would be much crossover between crowdfunded offerings in which securities are not offered or sold and those in which investment crowdfunding is conducted, the unregulated market that pre-existed the CROWDFUND Act indicates that there is some interest in the crowdfunding of unequity—which does constitute investment crowdfunding—by, and in a manner similar to that used by, issuers seeking funding through crowdfunding that does not involve the offer or sale of a security.¹²⁷

Commentators have begun to call on Congress to take action to rescue the crowdfunding exemption by, among other things, reducing the associated

124 See Campbell, *supra* note 21, at 836 (“The Commission in its first iteration of its crowdfunding regulations has failed to appreciate the impact on small issuers of the relative offering costs generated by the crowdfunding disclosure obligations.”).

125 See *id.* (“Especially adversely impacted . . . will be offerings by small business with small external capital needs, which seems exactly counter to the whole purpose of the JOBS Act.”).

126 See *supra* notes 78–82 and accompanying text.

127 See *supra* notes 78–82 and accompanying text.

costs. “In order for equity crowdfunding to the public to serve as a useful tool, as intended,” one observer wrote, “Congress needs to amend the JOBS Act to make it less onerous and costly.”¹²⁸ Another simply offered, “I think the Congress should start over.”¹²⁹ Rep. Patrick McHenry has introduced a bill in Congress that would essentially do just that: it supplants Title III of the JOBS Act and replaces it with a simpler, more efficient, registration exemption regime for investment crowdfunding.¹³⁰

I do not favor additional congressional action to alter the cost structure of the CROWDFUND Act as a means of affording relief to small private issuers desiring to make limited offerings over the Internet. Congress is not well equipped as a representative, diverse, highly political, non-expertized, legislative body to engage in the nuanced balancing of costs and benefits in the emergent crowdfunding market. This task is much more in the rulemaking wheelhouse of the SEC as an appointed, relatively nimble, less political, expert regulator.¹³¹

As a result, I suggest that the SEC return to the task of regulating crowdfunding to better address unmet and underserved needs in the market for small business capital. In my original coauthored paper on crowdfunding, my coauthor and I advocated a process by which the SEC could approach that work and outlined the possible substantive elements of resulting regulation.¹³² At the risk of inviting accusations that I am a one-trick pony or that I continue to incessantly beat a single drum, I urge the SEC to return to that process and those elements and propose an exemption from registration that employs a lower level of regulation and cost while correspondingly reducing investor risk.

A number of productive ideas could ensue. The ultimate regulatory outcome of that process could be, for instance, a new federal registration exemption featuring significantly lower per-unit and aggregate investor caps—a rule that limits investor risk by decreasing investor exposure to financial harm. With a rule of that kind, there should be fewer concerns the need for significant investor protection devices (e.g., detailed mandatory disclosures and enhanced liability provisions). Alternatively, engagement with the suggested rulemaking process could result in the SEC determining that unequity¹³³ should be re-classified as an instrument that is exempt from the definition of a security, ceding regulatory control of unequity transactions to consumer protection regulation.

¹²⁸ Korn, *supra* note 68.

¹²⁹ William Carleton, *The JOBS Act: A Better Way to Regulate Equity Crowdfunding*, VCEXPerts, https://vcexperts.com/buzz_articles/1303 (last visited Apr. 6, 2014).

¹³⁰ See Equity Crowdfunding Improvement Act of 2014, H.R. 4564, 113th Congress (2014), available at <https://www.govtrack.us/congress/bills/113/hr4564/text>.

¹³¹ Cf. Cohn, *supra* note 26, at 1445 (indicating that the SEC may have been best positioned, but unlikely, to balance the competing interests at stake in constructing an efficacious 1933 Act registration exemption for crowdfunding).

¹³² See Heminway & Hoffman, *supra* note 5, at 937–61.

¹³³ See *supra* notes 84–85 and accompanying text.

The SEC's task now must also take into account the CROWDFUND Act and the final form of its implementing rules. This should make its task easier (and make its participation more likely). In other words, this Article suggests that the SEC should regulate in the void left after full implementation of the CROWDFUND Act's registration exemption (which, at the time this Article was written, had not yet occurred) to establish a prudent, realizable regulatory exemption from 1933 Act registration for small crowdfunded offerings.

CONCLUSION

Among other things, the CROWDFUND Act in particular and the JOBS Act more generally respond to a natural expansion of private offerings beyond face-to-face and other directed communications between and among repeat players.

Market demand, the Internet, and new modes of communication are driving significant changes in capital markets. These changes put increasing pressure on federal and state policymakers to ensure that laws are not unnecessarily impeding the fair and efficient flow of capital. The 2012 JOBS Act was an important first step in recognizing these shifting dynamics, but more needs to be done to enhance capital access for businesses ranging from startups to more mature companies ready for the public markets.¹³⁴

Specifically, apropos of the theme of the symposium for which this Article was researched and written ("The Securities Act of 1933 at 80: Does It Provide a Fair and Efficient Access to Capital?"),¹³⁵ investment crowdfunding under the CROWDFUND Act is neither fair nor efficient. In its current form, the CROWDFUND Act provides, at best, a deep-discount, limited-use registration exemption under the 1933 Act. In its effort to deregulate investment crowdfunding, the CROWDFUND Act introduces new regulation and attendant costs to a magnitude and in a manner likely to drive many, if not most, small businesses to other capital formation methods.¹³⁶

However, hope (as they say) springs eternal. With the thought that all is not yet lost, this essay proposes (actually, *re*-proposes) an approach to a workable 1933 Act registration exemption for crowdfunded limited offerings. There are possible ways forward; but navigating these paths to a more fair and efficient system of investment crowdfunding will not be easy. They require abundant patience, sufficient skill, and ample political will, any or all of which may be

¹³⁴ Gorfine, *supra* note 123.

¹³⁵ Symposium, *The Securities Act of 1933 at 80: Does It Provide a Fair and Efficient Access to Capital?*, 102 Ky. L.J. 815 (2014), available at <http://www.law.uky.edu/index.php?pid=473>.

¹³⁶ See Campbell, *supra* note 21, at 848 ("Without significant changes, the crowdfunding will be less available for small business issuers than efficiency would require"); Hurt, *supra* note 21, at 46-48 (describing why "Equity Crowdfunding is Doomed Because Section 4(6) is Too Costly and Burdensome on Issuers and Portals"); *id.* at 59 ("Though crowdfunding has the promise of . . . democratizing both access to capital and access to investment opportunities, a shift from retail crowdfunding to accredited crowdfunding will not fulfill that promise.").

lacking in the near or foreseeable future. Nevertheless, the ideas shared are designed to provide the basis for, at a minimum, further constructive discussion about the desire for capital market expansion evidenced in the JOBS Act.

