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# The More the Merrier: SEC Amends Crowdfunding Rules to Increase Investment Limits

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## Westlaw/Corporate Alert

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On November 2, 2020, the Securities and Exchange Commission (SEC) voted to amend certain rules related to the issuance of securities in exempt offerings—transactions in which the securities sold by the issuer do not need to be registered with the SEC. Among these amendments are changes to rules affecting Regulation Crowdfunding (Reg CF), which allows eligible companies to offer and sell securities through regulated online crowdfunding portals. These amendments could significantly democratize fundraising for early stage companies by making it easier for them to raise more capital from the general public. The amendments will generally go into effect in early 2021.

The most notable amendment to Reg CF is an increase in the amount eligible companies can raise, from $1.07 million to $5 million in a twelve-month period. By allowing companies to raise nearly five times more capital, the SEC has made a Reg CF offering a more realistic alternative to Rule 506 of Regulation D—the exemption traditionally relied on by companies raising capital from private investors—for startups raising seed capital.

While the disclosure and ongoing reporting requirements for Reg CF offerings are generally more burdensome than for Rule 506 offerings, increasing the investment limit for Reg CF makes the additional cost of compliance less material, particularly for companies that would otherwise solicit investments from the public under Rule 506(c) or expect to include some non-accredited investors in an offering under Rule 506(b). While every early-stage company will need to evaluate the merits of raising capital via Reg CF based on its own circumstances, the increased limit is a welcome development that will expand access to capital.

In addition to increasing the dollar amount early stage companies can raise, the amendments make two significant changes to the amount an investor may invest in Reg CF offerings. For anyone who qualifies as an “accredited investor” under Rule 501 of Regulation D, there will no longer be a limit on the amount that can be invested in a company via a Reg CF offering. This further levels the playing field between offerings conducted under Reg CF and Rule 506 of Regulation D, which already has no investment limits for accredited investors.

For non-accredited investors, the limit on the amount that can be invested via Reg CF will now be the greater of (as opposed to lesser of, as under the current rule) existing limits that are based on the investor’s annual income or net worth. These amendments will further enhance the ability of companies to raise capital by permitting increased investment amounts from both accredited and non-accredited investors.

Finally, companies that wish to rely on Reg CF will soon have the ability to use generic solicitation of interest materials to “test the waters” before filing an offering document with the SEC, as is required when conducting a Reg CF offering. This change should significantly reduce the number of

Reg CF offerings that fail to reach their minimum fundraising target and, since preparing the offering document is typically the most time-consuming and costly step in a Reg CF offering, this change will also greatly reduce the amount of capital wasted on offerings that are ultimately unsuccessful.

These developments are welcome news for early stage companies. Not only will the amount of capital that can be raised under Reg CF increase nearly fivefold, but investor interest is also likely to be greater because of the increased investment limits. The ability to test the waters will allow companies a better opportunity to evaluate investor interest prior to incurring the bulk of the costs of a Reg CF offering. As the market for Reg CF grows, these developments may be viewed as a turning point in the democratization of access to capital and investment that will give early stage companies a better chance to build, grow and scale.