PUBLICATION

Federal Crowdfunding Efforts Stall While Tennessee Prepares for Takeoff

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On January 1, 2015, pursuant to the Invest Tennessee Exemption (ITE), crowdfunding in Tennessee became legal, granting Tennessee-based companies and investors increased access to capital and broadened opportunities to invest. Federal crowdfunding rules, however, are stalled again—now delayed by more than 700 days past the deadline required by 2012's Jumpstart Our Business Startups Act (the JOBS Act). The Chairwoman of the Securities and Exchange Commission (SEC), Mary Jo White, indicated that the SEC is "actively working through" the proposed crowdfunding rules, but nothing would be finalized until late 2015. Thus, the rules will not be available to companies and investors until early 2016.

Typically, a company seeking to sell securities to investors must either *register* the sale of its securities with the SEC and any applicable state securities authority, or find an available *exemption* from such registration. At the Federal level, there are various exemptions available, but the ITE requires that the offering comply with the intrastate offering exemption under Section 3(a)(11) of the Securities Act of 1933, as amended, which permits companies organized and operating in a particular state to sell to residents of that state without registering the sale of securities with the SEC. Before January 1, 2015, a company seeking to rely on the Federal intrastate offering exemption would nevertheless have been required to register with the Tennessee Department of Commerce and Insurance (TDCI). The ITE eliminated the requirement that a company register with TDCI, *if* the company conforms to certain conditions, effective January 1, 2015.

If a company complies with those conditions, the ITE permits the company to:

- Offer its securities for sale to Tennessee-based investors by general solicitation and advertisement, reaching out to Tennessee residents through traditional print and broadcast media, as well as through start-up investment platforms and via social media.
- Accept subscriptions from unaccredited investors up to $10,000 (in addition to unlimited amounts from accredited investors).
- Raise up to $1 million during a 12-month period.

One of the authors of the bill highlighted the ITE's potential with respect to Tennessee's vibrant start-up culture, noting that crowdfunding could act as a platform for some businesses, and could possibly spur community development. Nevertheless, some industry commentators believe that it is unlikely that the ITE will have a substantial impact, and that the costs of compliance with legal requirements may undercut any prospective benefits.

Although Tennessee has forged ahead with its efforts to expand investment opportunities through crowdfunding, Federal efforts have stalled. Most legal experts and industry insiders had expected the rules to be finalized in 2014, but Title III of the JOBS Act, which would allow small businesses to use Internet-based crowdfunding platforms to raise up to $1 million from both accredited and unaccredited investors, is now not expected to be finalized until sometime in October 2015 per the SEC's published agenda with respect to upcoming rulemaking. Some commentators, however, have viewed this delay in a positive light, hoping that the various state laws concerning crowdfunding, over a dozen in all, will reveal the best way to both expand investment opportunities and protect investors in the process.

To discuss the impact of the ITE or the delay of the Federal crowdfunding rules on your business, please contact your Baker Donelson attorney or a member of our Securities and Corporate Governance Group.