Stradling
Attorneys at Law

A Year End Look at Equity Crowdfunding in the US: 2017

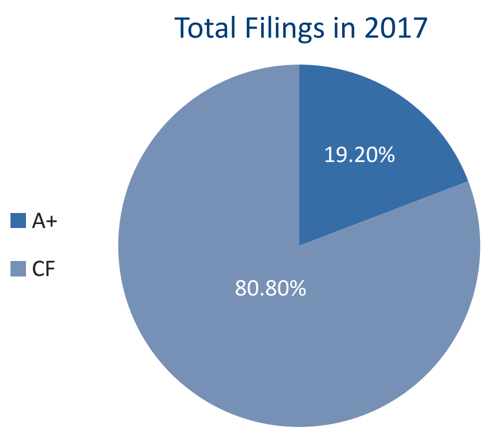
A Year End Look at Equity Crowdfunding in the US: 2017

Stradling
Attorneys at Law

Overview of Results

The 2012 Jumpstart Our Business Startups (JOBS) Act established provisions that allow early-stage companies to offer and sell securities to the public with relatively light regulation. Both Regulation A+ and Regulation Crowdfunding help startups crowdfund equity investments from unaccredited and accredited investors. While the regulations were adopted in 2015, offerings under these rules gained significant traction in 2017.

- From January through December 2017, 636 companies filed forms to conduct new offerings under Regulation A+ or Regulation Crowdfunding. The latter was the more widely used, with 80 percent of those issuers conducting a Regulation Crowdfunding offering.



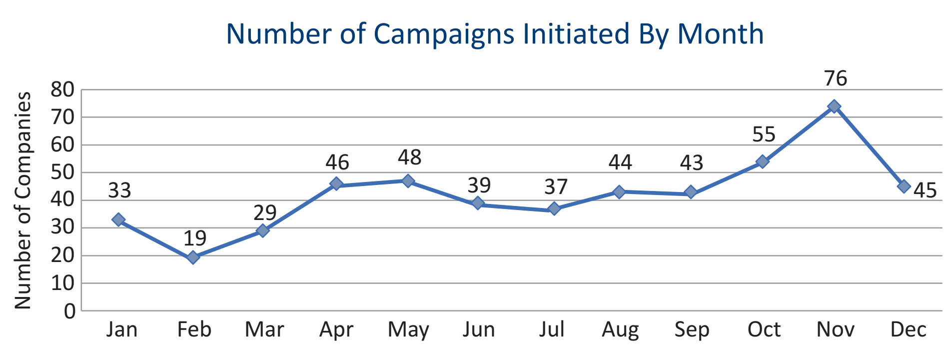
- Approximately 47 percent of the companies that submitted filings under Regulation Crowdfunding were incorporated in the state of Delaware, in comparison to nearly 57 percent of the issuers to conduct a Regulation A+ offering were incorporated in that state.

- Common stock and debt accounted for 37 percent and 26 percent, respectively, of the offerings under Regulation Crowdfunding, while Simple Agreements for Future Equity (SAFEs) were issued in just over 22 percent of the offerings. In contrast, common stock was issued in 81 percent of Regulation A+ offerings. This makes sense since Regulation A+ allows companies to conduct mini initial public offerings (IPOs) and virtually all IPOs are common stock issuances.

Regulation CF

Regulation CF allows private companies to offer and sell up to $1 million of securities to accredited and unaccredited investors through crowdfunding offerings over a 12-month period, under certain conditions. The issuer is required to conduct its offering through an online platform operated by an intermediary that is registered with the SEC either as a broker-dealer or as a funding portal.

Over the course of 2017, there were 514 initial Form C filings submitted to the SEC to conduct a Regulation CF offering. The level of activity was higher in the second half of the year than the first, bolstered by 4Q2017, in which there were 176 initial filings. This was the most of any single quarter since the regulation took effect in May 2016. The month of November, in particular, saw a good deal of activity with 76 initial filings.

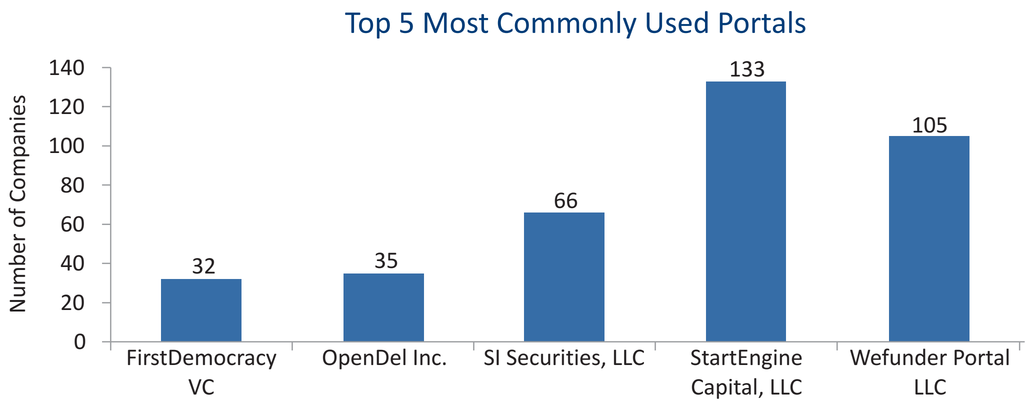


Because the issuer must raise at least the target amount to receive funds, the typical offering sets both a target and a maximum amount, increasing the likelihood of raising at least some funding while preserving the flexibility to raise up to a higher limit. The average minimum amount sought to be raised by the companies that submitted initial filings in 2017 was just under $73,825. The average maximum amount targeted was approximately $596,580.

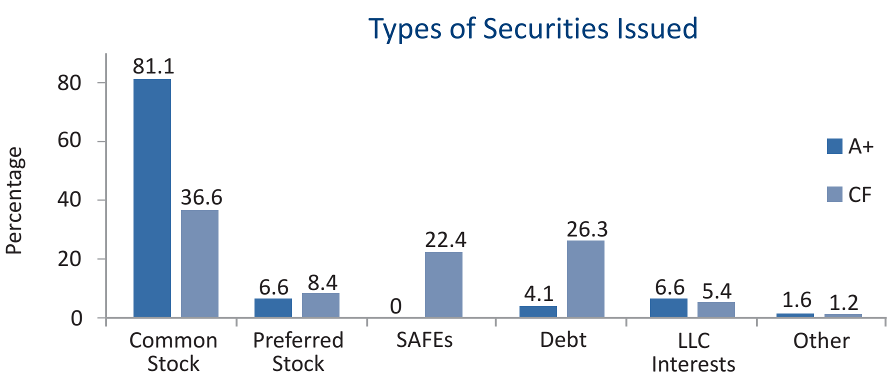
Amounts Requested and Raised

Of those companies that submitted initial filings, 126 reported the amount raised through Form C-U, which is required upon completion of the offering. In total, these companies raised more than $33.2 million, more than $25 million of which was reported in the final six months of 2017. The average amount raised per company was approximately $264,160. The maximum amount raised by any one issuer during that period was $1.07 million; the minimum was $10,500.

Intermediaries



The vast majority of offerings involved funding portals, as opposed to broker-dealers. Although more than two dozen portals participated in Regulation Crowdfunding in 2017, the five largest portals based on the number of offerings accounted for 72 percent of the initiated offerings. StartEngine Capital LLC was the most widely used, having taken part in 133 offerings. It was followed by Wefunder Portal LLC, which was used by 105 companies. SI Securities was a distant third, taking part in 66 offerings.

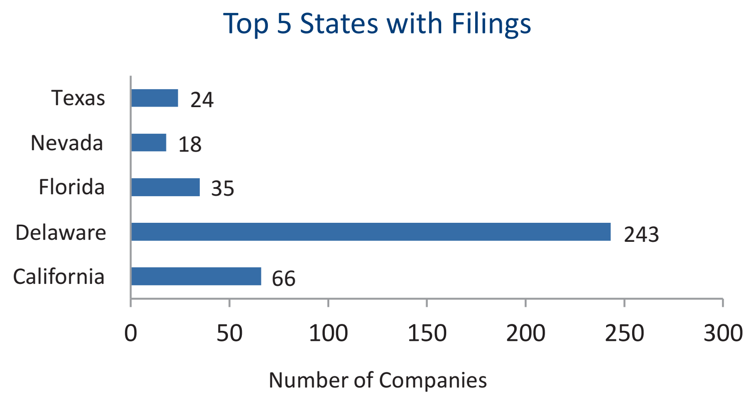


Types of Securities

The most popular type of security was equity, either in the form of common stock or preferred stock. Common stock was issued in over 36 percent of the offerings, while preferred stock was issued in approximately 8 percent of the offerings. Convertible debt was the second most widely-used, at 26 percent. SAFEs, a popular investing tool used as an alternative to convertible debt, accounted for roughly 22 percent of offerings. This is comparable to the Regulation Crowdfunding activity in 2016, as reported by the SEC, though debt surpassed SAFEs in popularity in 2017.

State of Incorporation

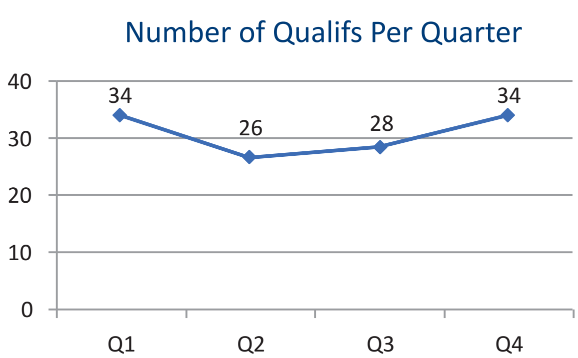
To be eligible to use the Regulation Crowdfunding exemption, companies must be based in the United States. The most common state of incorporation for companies that submitted initial filings was Delaware. Companies from that state were responsible for 243 filings, or 47 percent of all filings. California was a distant second with 66, followed by Florida and Texas, which had 35 and 24 filings, respectively. While 37 of the 50 states were represented, the top five states accounted for over 75 percent of the filings.



Industry

Of the companies that utilized Regulation Crowdfunding, 204, or almost 40 percent, were in the technology industry. Companies in the life science and real estate industries represented about six percent of the filings. The remaining 54 percent was made up of companies in other industries.

Regulation A+



Regulation A+, also known as Title IV of the JOBS Act, allows companies to raise up to $50 million in a 12-month period from both accredited and unaccredited investors. This regulation is similar to a traditional IPO, but with more limited disclosure requirements than a full-fledged IPO. Regulation A+, which took effect in June 2015, provides for two tiers of offerings: Tier 1 for offerings of securities up to $20 million; and Tier 2 for offerings of up to $50 million.

Much like an IPO, Regulation A+ offerings must be qualified by the SEC before issuers may sell securities. In 2017, there were 122 qualified Regulation A+ offerings filed by prospective issuers. Tier 2 offerings comprised approximately 80 percent of the qualified offerings. The total number of qualified offerings was relatively consistent between the first and second halves of 2017, with 60 and 62 filings, respectively.

Types of Securities

Common stock was by far the most common type of security, issued in more than 81 percent of the offerings. Preferred stock and convertible debt were issued in approximately six percent and four percent, respectively. LLC Units and other forms of securities accounted for the remainder of the securities issued. This is in line with numbers reported by the SEC capturing the period between June 2015 and October 2016, in which equity accounted for 87 percent of securities issued in all offering statements.

Amount Raised

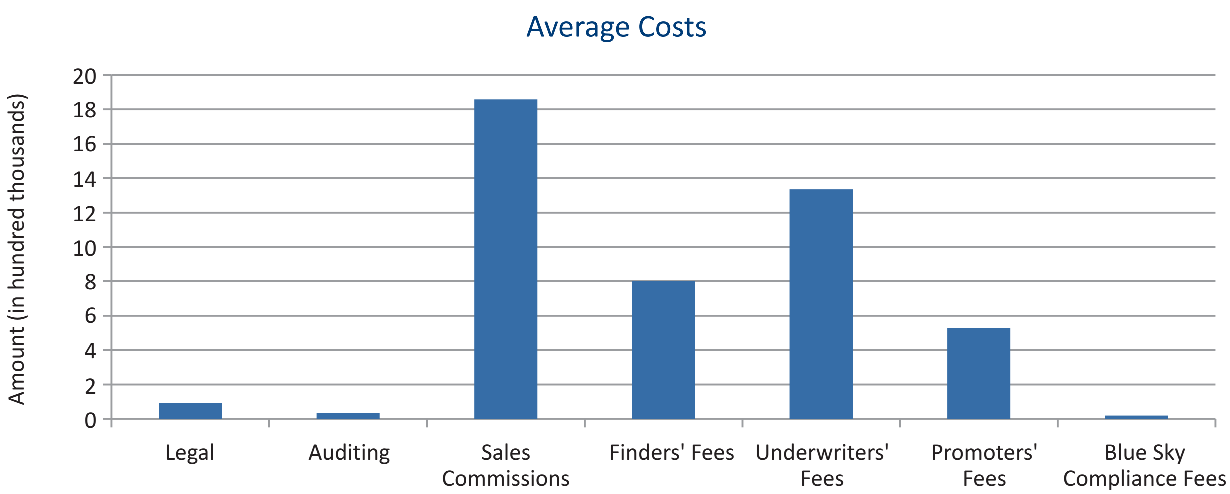
Of those companies that filed statements for qualified offerings, 13 reported the amount raised through a Form 1-U. In total, these companies collectively raised more than $236.5 million. The average amount raised per company was approximately $18.2 million. The maximum amount raised by any one issuer during that period was $55.6 million; the minimum was $174,862.

State of Incorporation

Delaware was the state of incorporation for 69 companies that submitted filings under Regulation A+, accounting for 56 percent of the filings. Nevada was the only other state with more than 10 filings. Wyoming and Maryland each had 7, followed by Florida (5) and California (4).

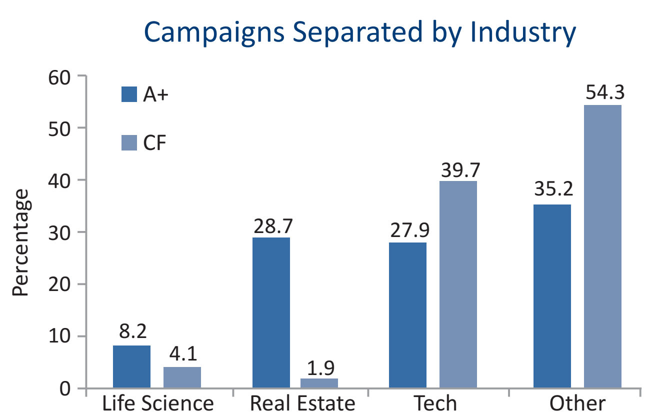
Offering Costs

The average company that reported costs associated with a Regulation A+ offering spent just over $93,000 in legal fees. The average audit cost was reported as approximately $33,735. Significantly fewer companies reported costs associated with remaining fees. From the limited data available, the average costs were as follows: sales commissions, $1.8 million; finders' fees, $800,000; underwriters' fees, $1.3 million; promoters' fees, $529,630; and Blue Sky compliance fees, $19,819.



Industry

The technology and real estate industries were fairly evenly represented among companies that submitted filings under Regulation A+; 34 were in the tech sector and 35 in real estate. Life science companies filed 10 statements for qualified offerings. The remaining 43 companies were in other industries.



Stradling
Attorneys at Law

Summary

In recent years, crowdfunding websites like Kickstarter and GoFundMe have become a popular way for people to solicit charitable contributions or raise money for projects. Now, companies can use crowdfunding for a whole new purpose: to offer and sell securities to the investing public. Anyone has the ability to invest in these companies, something that has traditionally been reserved for the elite few. For startups, it provides another fundraising avenue, a benefit particularly for those unable to obtain seed financing from angel or venture capital investors. Though the numbers here are very small compared with the funds received through IPOs and even traditional private offerings, as companies and their attorneys acclimate to the new regulatory environment, these relatively new regulations will likely play an outsize role in companies' future funding plans.

About the Author

Amit Singh is a shareholder in Stradling's corporate and securities law and technology transactions practice groups. He has practiced corporate law for more than 19 years and is a corporate governance and business transactions expert, with extensive experience in venture capital and private equity transactions, mergers and acquisitions, joint ventures, technology transactions and general corporate law. Amit counsels companies and investors in a broad range of industries, including life sciences, software, hardware, communications and networking, internet, manufacturing and distribution and medical devices. Special thanks to Peter Hong and Arash Lessantiz for their contributions.

About Stradling

Founded in Newport Beach by four attorneys in 1975, Stradling has grown to more than 130 attorneys in nine offices across California, Colorado, Nevada and Washington. Originally a corporate law boutique, Stradling now offers a wide range of legal services. Our attorneys specialize in areas as diverse as corporate transactions, securities and complex business litigation, tax, intellectual property, employment, real estate, public law and municipal finance. This enables us to represent some of California's leading companies and municipalities in a broad array of complex and sophisticated matters.

SYCR.COM
(949) 725-4000

Newport Beach | Denver | Reno | Sacramento | San Diego | San Francisco | Santa Barbara | Santa Monica | Seattle

Contact/Sign Up Information

For additional information about this report please contact Amit Singh at (858) 926-3012; asingh@sycr.com at Stradling.

To view the report and a chart that includes our research, please visit: sycr.com/a-year-end-look-at-equity-crowdfunding-in-the-us-2017.

To be placed on an email list for future editions of this report please email sfeuchter@sycr.com.

Disclaimer

The preparation of the information contained herein involves assumptions, compilations and analysis, and there can be no assurance that the information provided herein is error-free. Neither Stradling Yocca Carlson & Rauth, P.C. nor any of its partners, associates, staff or agents shall have any liability for any information contained herein, including any errors or incompleteness. The contents of this report are not intended, and should not be considered, as legal advice or opinion. To the extent that any views on equity crowfunding or other matters expressed in this report, they are the views of the author only, and not Stradling Yocca Carlson & Rauth, P.C.