ThinkAdvisor

SEC Amends Capital-Raising Rules

November 03, 2020

Melanie Waddell

"These changes do little to ease the costs of capital for the smallest companies," said Cato's Schulp.

The Securities and Exchange Commission **voted Monday to amend** its capital-raising rules for small and medium-sized businesses.

"For many small and medium-sized business, our exempt offering framework is the only viable channel for raising capital. These businesses and their prospective investors must navigate a system of multiple exemptions and safe harbors, each with different requirements," said SEC Chairman Jay Clayton in a statement. "While each component in this patchwork system makes some sense in isolation, collectively, there is substantial room for improvement."

SEC staff, Clayton added, "identified various costly and unnecessary frictions and uncertainties, and crafted amendments that address those inefficiencies in the context of a more rational framework that will facilitate capital formation for small and medium-sized businesses and benefit investors for years to come."

Jennifer Schulp, director of financial regulation studies for the libertarian-leaning Cato Institute, said in an email to ThinkAdvisor that while the amendments "are a welcome step to streamline the exceedingly complex capital raising rules. … these changes do little to ease the costs of capital for the smallest companies seeking to use Regulation Crowdfunding, who can find the rules impose a comparatively hefty cost on a smaller dollar offering."

Raising the crowdfunding offering limit to $5 million, "as the SEC did, may draw more companies looking to raise larger amounts of capital, but more work needs to be done to help the smallest companies take advantage of this exemption," Schulp said.

Related: SEC Gives Break on Crowdfunding Rules for Some Small Firms

The commission is amending the current offering and investment limits for certain exemptions.

For Regulation A, the amendments:

- Raise the maximum offering amount under Tier 2 of Regulation A from $50 million to $75 million; and
- Raise the maximum offering amount for secondary sales under Tier 2 of Regulation A from $15 million to $22.5 million.

For Regulation Crowdfunding, the amendments:

- Raise the offering limit in Regulation Crowdfunding from $1.07 million to $5 million;
- Amend the investment limits for investors in Regulation Crowdfunding offerings by:
    - Removing investment limits for accredited investors; and
    - Using the greater of their annual income or net worth when calculating the investment limits for non-accredited investors; and
- Extend for 18 months the existing temporary relief providing an exemption from certain Regulation Crowdfunding financial statement review requirements for issuers offering $250,000 or less of securities in reliance on the exemption within a 12-month period.

Democratic commissioners Allison Herren Lee and Caroline Crenshaw dissented.

"My concerns with the individual provisions of the final rule are numerous," Lee said. "I question, for example, the wisdom of increasing capital raising limits in offerings such as Regulation A, Crowdfunding, and Rule 504 when investors have demonstrated no interest, and issuers no need, for such increases."

A "larger concern," she continued, "is the sweeping effect of these changes taken together and in the broader regulatory context, including the commission's failure to address the effects of inflation on the nearly 40-year-old wealth thresholds in the accredited investor definition. Because of the commission's failure to modernize these wealth thresholds, the pool of accredited investors is getting steadily bigger and the investors in that pool steadily less wealthy."

Crenshaw stated that the new rules "will significantly expand private market access to investors without first putting in place appropriate investor protections. Under these rules, private companies would be allowed to raise capital by selling more risky offerings, in greater dollar amounts, with less information, and fewer rights, to retail investors."