



newsletter

FINRA Issues Guidance to Broker-Dealers on Crowdfunding

By Andrew J. Dorman and Brian P. Nally



On January 29, 2016, FINRA Rule 4518 – governing recent changes in the world of crowdfunding – became effective. FINRA Regulatory Notice 16-07 provides guidance on the rule and to broker-dealers who are contemplating acting as intermediaries in crowdfunding portals.

By way of background, President Obama passed into law the Jumpstart Our Business Startups Act (JOBS Act) on April 5, 2012. One goal of the JOBS Act was to increase American job creation and economic growth by facilitating investment into small business and start-up companies. To this end, Section 201(a) (2) of the JOBS Act directed the SEC to remove the long-standing prohibition on general solicitation or general advertising for securities offerings relying on Rule 506. The SEC proposed such a rule in August of 2012, provided that the sales of securities would be limited to accredited investors and that issuers would be required to take reasonable steps to verify such accredited status. A final version of this proposal

was approved on July 10, 2013 and made effective 60 days later. The final version of the rule removed the ban on general solicitations and permitted issuers relying on a Rule 506 exemptions to use general solicitation and general advertising to offer their securities, provided that: (1) the issuer takes reasonable steps to verify that the investors are accredited investors; (2) all purchasers of the securities fall within one of the categories of persons who are accredited investors under an existing rule (Rule 501 of Regulation D) or the issuer reasonably believes that the investors fall within one of the categories at the time of the sale of the securities. Small businesses and start-ups could for the first time raise funds from the general

public through general solicitations, so long as the individuals who actually invest are properly vetted and determined to be accredited.

In October of last year, the SEC again passed a rule under the JOBS Act, this time permitting companies to offer and sell securities through crowdfunding. Crowdfunding is the method by which companies, particularly start-up companies, can raise capital through the Internet. Under the final rule, a company can raise a maximum aggregate amount of \$1M over a 12-month period subject to certain restrictions placed on the

individual investors. A funding portal, a company acting as the intermediary between the company and an investor, would be required to register with the SEC as a new Form Funding Portal, and become registered with FINRA. Under FINRA Rule 4518, effective January 29, 2016, a FINRA member that intends on acting as a funding portal must notify FINRA (1) prior to engaging, for the first time, in a transaction involving the offer or sale of securities in reliance on the crowdfunding exemption; or (2) within 30 days of directly or indirectly controlling, or being controlled by or under common control with, a funding portal. Specifically,

member firms must visit the FINRA Firm Gateway and update their profile information, and in some instances, may need to apply for approval of a material change in business operations pursuant to NASD Rule 1017.

Crowdfunding will be a hot-button issue for many years to come. Be sure to carefully consider all applicable rules and regulations before engaging in any activities. To review Regulatory Notice 16-07 in full, click on the following link: <https://www.finra.org/sites/default/files/Regulatory-Notice-16-07.pdf>

About the Authors: Andrew J. Dorman (Chair) and Brian P. Nally (Member) are attorneys in the Financial Services Professional Liability practice group of Reminger Co., L.P.A., with offices in Ohio, Kentucky, and Indiana.

This has been prepared for informational purposes only. It does not contain legal advice or legal opinion and should not be relied upon for individual situations. Nothing herein creates an attorney-client relationship between the Reader and Reminger. The information in this document is subject to change and the Reader should not rely on the statements in this document without first consulting legal counsel.

AKRON 400 Courtyard Square • 80 South Summit Street • Akron, Ohio 44308 • (330) 375-1311

CINCINNATI 525 Vine Street • Suite 1700 • Cincinnati, Ohio 45202 • (513) 721-1311

CLEVELAND 101 West Prospect Avenue • Suite 1400 • Cleveland, Ohio 44115 • (216) 687-1311

COLUMBUS Capitol Square Office Bldg. • 65 East State Street, 4th Floor • Columbus, Ohio 43215 • (614) 228-1311

SANDUSKY 237 W. Washington Row, 2nd Floor • Sandusky, Ohio 44870 • (419) 609-1311

TOLEDO One SeaGate • Suite 1600 • Toledo, Ohio 43604 • (419) 254-1311

YOUNGSTOWN 11 Federal Plaza Central • Suite 1200 • Youngstown, Ohio 44503 • (330) 744-1311

FT. MITCHELL 250 Grandview Drive • Suite 550 • Ft. Mitchell, Kentucky 41017 • (859) 426-7222

LEXINGTON Vine Center • 333 West Vine Street, Suite 1670 • Lexington, Kentucky 40507 • (859) 233-1311

LOUISVILLE 730 West Main Street • Suite 300 • Louisville, Kentucky 40202 • (502) 584-1310

INDIANAPOLIS Three Parkwood • Suite 150 • 450 E. 96th Street • Indianapolis, Indiana 46240 • (317) 663-8570

FORT WAYNE Lincoln Tower 116 East Berry • Street Suite 1735 • Ft. Wayne, Indiana 46802 • (260) 755-2280

NORTHWEST INDIANA One Professional Center, Suite 315 • 2100 North Main Street • Crown Point, Indiana 46307 • (219) 663-3011

