

## Crowdfunding

*The Internet is a popular way for individuals and businesses to raise money. In 2012, Congress passed the JOBS Act, which directed the Securities and Exchange Commission (SEC) to formulate rules to exempt investment crowdfunding from the securities registration laws. These rules went into effect in May 2016 and eased restrictions on start-up companies that use the internet to find investors.*

### **What is Investment Crowdfunding?**

At its core, investment crowdfunding is a method of raising capital from a large number of people who each invest relatively small amounts of money. Securities sold in this way rely on federal and state securities registration exemptions. With investment crowdfunding, investors buy a “security” issued by the company with the expectation of some type of financial return. They often receive ownership or creditor rights in the company. Investment crowdfunding is not to be confused with donations-based or rewards-based crowdfunding where no securities are offered.

While the SEC rules apply to crowdfunding on the national level, many states have enacted their own intrastate crowdfunding laws. Now small businesses in those states have the option to use state-based crowdfunding exemptions to raise capital from investors within their jurisdiction’s borders.

To date, nearly two-thirds of the states and the District of Columbia, including Virginia have laws on the books that allow businesses in their jurisdictions to raise money through state-based crowdfunding.

*(revised: August 2017)*

### **How Crowdfunding Works**

Traditionally, investment opportunities are offered by professionals, such as broker-dealer firms and investment advisers, who must recommend investments that are based on their clients’ investment objectives and levels of sophistication.

Through crowdfunding, individuals can invest in entrepreneurial start-ups using an intermediary, such as a broker-dealer or a “funding portal.” By law, “funding portals” are not allowed to provide investment advice.

For example, Joe owns a business that sells cheese. To help his business grow, Joe goes online to seek investors using a funding portal. Joe needs to comply with applicable state and/or federal laws that govern crowdfunding exemptions for the offer and sale of securities.

Depending on how Joe structures his offering, he can issue equity interests in his company or a debt instrument, and will be expected to provide a financial return on the investment.

#### **To learn more, contact:**

STATE CORPORATION COMMISSION, DIVISION OF SECURITIES AND RETAIL FRANCHISING,  
1300 EAST MAIN STREET, RICHMOND, VA 23219, [WWW.SCC.VIRGINIA.GOV/SRF](http://WWW.SCC.VIRGINIA.GOV/SRF), 800-552-7945



## Who Can Invest?

Investment crowdfunding is not limited to wealthy or financially sophisticated investors. In fact, anyone can invest in a crowd-funded securities offering. But investors must remember that all investments come with risks. Investors should learn as much as they can about the investment and the company and carefully read all of the disclosures.

## Federal and State Crowdfunding

*Under the SEC's rules and federal crowdfunding, businesses can raise up to \$1.07 million in a 12-month period from individual investors, who can invest amounts ranging from \$2,000 to \$107,000 in a 12-month period depending on their income and net worth. Offerings must be conducted online through a broker-dealer or funding portal.*

*Under state crowdfunding laws, businesses can raise money from local investors directly or through a broker-dealer or funding portal. The amount a business can raise, and individual investment limits, are determined by each state's crowdfunding laws. For more information about crowdfunding in Virginia, please visit <http://law.lis.virginia.gov/admincode/title21/agency5/chapter40/section190/>.*

## Crowdfunding Considerations for Investors

- All investments have risk, but small business investments are particularly risky. Small businesses have high failure rates and there is very little information publicly available about the businesses. Investors should be prepared to lose their entire investment.
- Crowdfunding portals or other online intermediaries claiming an accreditation or "seal of approval" from a standards program or board may not be legitimate.
- Issuers using funding portals to raise money may be inexperienced. Their track records may be unproven, unsubstantiated or outright fraudulent.
- Investors should rely on their own research to determine an issuer's track record and review an issuer's disclosures carefully.
- Crowdfunding investments are mostly illiquid and investors must be prepared to hold their investments indefinitely. It may be difficult or impossible to resell these securities due to the lack of a secondary market.

## The Bottom Line



While crowdfunding opens new capital raising opportunities for small businesses and investors, you should perform due diligence on investment opportunities you learn about through the Internet. When you see an offering on the Internet — whether on a funding portal, in an online newsletter, message board or chat room — you should do your homework. For questions about crowdfunding offerings, contact the Virginia Division of Securities and Retail Franchising at [www.scc.virginia.gov/srf](http://www.scc.virginia.gov/srf) or 800-552-7945.