

Crowdfunding in Arkansas? Yes, you can!

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Following enactment of the Jumpstart Our Business Startups Act (also known as the JOBS Act)¹ in 2012, the SEC expanded the options for issuers seeking an exemption from the registration requirement for the sale of securities under federal law, while simultaneously preempting inconsistent state law.² One such innovation was Regulation Crowdfunding, generally referred to as Reg. CF,³ which currently allows compliant issuers to raise up to \$1,070,000 in any 12-month period⁴ by seeking relatively small investments from a large number of investors.⁵

The Federal Approach (Reg. CF)

There are, however, a number of rules applicable to Reg. CF offerings under federal law that make it a relatively cumbersome process, thereby limiting its utility.⁶ First, the SEC requires that all transactions under Reg. CF take place online through an SEC-registered intermediary, either a registered broker-dealer or funding portal.⁷ This can serve to significantly increase the expense associated with the offering.⁸ While the issuer in a

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1. Jumpstart Our Business Startups Act, Pub. L. No. 112-106, 126 Stat. 306 (2012).

2. *Exempt Offerings*, U.S. SEC. EXCH. COMM'N, <https://www.sec.gov/smallbusiness/exemptofferings> (last visited Nov. 9, 2018) [<https://perma.cc/B835-TLSF>].

3. Regulation Crowdfunding is authorized at 17 C.F.R. pt. 227 (2018). For an explanation of the terms and provisions of regulation crowdfunding, see *Regulation Crowdfunding: A Small Entity Compliance Guide for Issuers*, U.S. SEC. EXCH. COMM'N, (May 13, 2016), <https://www.sec.gov/info/smallbus/sec/rccomplianceguide-051316.htm> [hereinafter "*Crowdfunding Guide*"] [<https://perma.cc/5QK3-M4AR>]. As noted in the text, this regulation is often abbreviated as Reg. CF, and that convention will be adopted in this article as well.

4. 17 C.F.R. § 227.100(a)(1) (2017).

5. See 17 C.F.R. § 227.100(a)(2) (2017).

6. See *Crowdfunding Guide*, *supra* note 3.

7. 17 C.F.R. § 227.100(a)(3) (2017).

8. One list of expenses suggests that access to a regulated portal will generally range between 3% to 6% of the total capital raised. Lou Bevilacqua, *How Much Does It Cost To*

crowdfunding deal may sell to anyone (investors need not be accredited),⁹ the amount that individual investors can invest across all crowdfunding offerings in a 12-month period is strictly limited.¹⁰ For some, the limit may be as low as \$2,200 across all crowdfunding offerings in any 12-month period, but the maximum permissible investment changes with the income or assets of each investor.¹¹ Even accredited investors are limited in how much they may invest in any 12-month period.¹² Federal rules also require comprehensive disclosures to the SEC, to investors, and to the intermediary facilitating the offering.¹³ In addition, after a Reg. CF offering closes, the issuer will find itself subject to ongoing reporting requirements.¹⁴

Raise Money Through Equity Crowdfunding?, BEVILACQUA LEGAL BLOG (Sept. 26, 2016), <https://www.bevilacquapllegal.com/much-cost-raise-money-equity-crowdfunding/> (last visited Feb. 02, 2019) [<https://perma.cc/4ZWW-3ZZU>]. A list of regulated funding portals can be found online at <https://www.finra.org/about/funding-portals-we-regulate> (last visited Feb. 02, 2019) [<https://perma.cc/8FX5-4ZBV>].

9. “Accredited investor” is a term of art that is used and defined in Regulation D, which is codified at 17 C.F.R. §§ 230.501 through 230.508 (2017). In essence, accredited investors are wealthy and presumptively sophisticated businesses or individuals, or are persons serving as executive officers or decision-makers for the issuer. *See* 17 C.F.R. § 230.501(a) (2017). To illustrate, one option for being classified as accredited requires an individual to have a net worth (either alone or with a spouse) of at least \$1,000,000 (excluding the value of the person’s primary personal residence). 17 C.F.R. § 230.501(a)(5) (2017).

10. 17 C.F.R. § 227.100(a)(2) (2017). The SEC Crowdfunding Guide includes a table setting out the maximum allowed investments. *See Crowdfunding Guide, supra* note 3. Some investors will be limited to a maximum investment of \$2,200 across all crowdfunding offerings in any 12-month period, and no investor may invest more than \$107,000 in that time period. *Id.*

11. Reg. CF caps the maximum investment from any purchaser at the greater of \$2,200 or 5% of the lesser of the investor’s annual income or net worth if either the investor’s annual income or net worth is less than \$107,000, or 10% of the lesser of such amounts if both exceed \$107,000, reduced by amounts paid to all other issuers in the preceding 12 months. 17 C.F.R. § 227.100(a)(2) (2017).

12. Under 17 C.F.R. § 227.100(a)(2)(ii) (2017), the maximum that can be invested by anyone is \$107,000.

13. 17 C.F.R. § 227.201 (2018) (initial disclosures); and 17 C.F.R. § 227.203 (2018) (filing requirements and referencing Form C, required under 17 C.F.R. § 239.900). A copy of SEC Form C is available online at <https://www.sec.gov/files/formc.pdf> (last visited Feb. 02, 2019) [<https://perma.cc/JW8S-GBPA>]. The form itself has an option question and answer format, but regardless of whether that format is used, the information must be provided to the SEC and all prospective purchasers.

14. 17 C.F.R. § 227.202 (2018). On-going reporting requirements are almost as burdensome as the initial Form C requirements, and include all informational items described in § 227.201 (a), (b), (c), (d), (e), (f), (m), (p), (q), (r), and (x).

There are other requirements associated with Reg. CF,¹⁵ but one nice thing about crowdfunding is that anyone can buy in—the exemption is not limited to accredited investors.¹⁶ Another potential advantage is that the SEC has made it clear that they do not anticipate that Reg. CF offerings will be “integrated”¹⁷ into other exempt offerings.¹⁸ That means that an issuer can conduct a side-by-side or concurrent Reg. CF offering with an offering under Reg. D or Reg. A.¹⁹ Finally, an offer that meets all of the

15. For example, there are limits on advertising. 17 C.F.R. § 227.204 (2016). Reg. CF offerings are also subject to “bad actor” disqualification provisions. 17 C.F.R. § 227.202 (2018). The SEC Compliance Guide lists who is covered by the so-called “bad boy” provisions and the kinds of disqualifying events that can render the exemption unavailable. *Crowdfunding Guide*, *supra* note 3. The requirements listed here are intended to be descriptive rather than exhaustive.

16. Mark Roderick, *Crowdfunding for Accredited and Non-accredited Investors*, NAT'L ASS'N OF INDUS. AND OFFICE PROPS. (2015), <https://www.naiop.org/en/Magazine/2015/Summer-2015/Finance/Crowdfunding-for-Accredited-and-Nonaccredited-Investors> [<https://perma.cc/ZX7L-LE26>].

17. “Integration” means that sales of the same kind of security, undertaken at or about the same time, for the same general purposes, pursuant to a single plan of financing, are likely to be treated as part of a single offering. That would mean that every sale would have to comply with the terms of the exemption for the offering into which it is being integrated. However, although offers under Reg. CF will not be integrated with offers made under another exemption such as Reg. D, an issuer must take care that if the other exemption prohibits general solicitation (as would be the case with Rule 506(b)), purchasers in that offering may not be solicited by the Reg. CF offering. Similarly, if the other exemption allows for general solicitation (for example under Rule 506(c)), then those general solicitations may not include advertisements that would be prohibited under a Reg. CF offering.

One commentator has suggested that “[i]t seems likely that ‘side-by-side’ offerings, made to ‘accredited’ investors under Rule 506(b) or 506(c) alongside offerings to unaccredited friends and family in reliance on Section 4(a)(6), will become popular.” Peter Thomson, *Regulation Crowdfunding Rules*, SEEDINVEST BLOG (Sept. 21, 2016), <https://www.seedinvest.com/blog/crowdfunding/regulation-crowdfunding-rules> (last visited Feb. 02, 2019) [<https://perma.cc/G348-PYAW>].

18. While an issuer is required to aggregate amounts sold by the issuer or its affiliates in other Reg. CF offerings, “[a]n issuer should not include amounts sold in other exempt offerings during the preceding 12-month period.” Crowdfunding Final Rule, 80 Fed. Reg. 71392 (Nov. 16, 2015). In addition, “an offering made in reliance on Section 4(a)(6) should not be integrated with another exempt offering made by the issuer, provided that each offering complies with the requirements of the applicable exemption that is being relied upon for the particular offering.” *Id.* Under these principles, if the Reg. CF offering is followed by a Rule 506(b) or Rule 506(c) offering, the issuer will have to be careful about what is disclosed, and to whom. *Id.* For a greater discussion of the limits on concurrent offerings, see *Concurrent Online Offerings*, CROWDCHECK, <https://crowdcheck.com/sites/default/files/Concurrent%20online%20offerings.pdf> (last visited Feb. 02, 2019) [<https://perma.cc/68HR-3HP4>].

19. See Crowdfunding Final Rule, 80 Fed. Reg. 71392 (Nov. 16, 2015); see also Thomson, *supra* note 17.

requirements of the federal Reg. CF need not comply with state law, which is preempted under the new provisions.²⁰

Nonetheless, there appears to be significant concern that as currently configured, the federal crowdfunding process is too complex.²¹ One source opined that the reason for Reg. CF's "slow start" was the "high regulatory burdens and costs on startups and businesses attempting to raise funds" under Reg. CF.²² This raises

20. Preemption of inconsistent state regulation for certain federal exemptions dates back to 1996, when Congress enacted the National Securities and Markets Improvement Act of 1996 (NSMIA). National Securities and Markets Improvement Act of 1996, Pub. L. No. 104-290, 110 Stat. 3416 (codified as amended in scattered sections of 15 U.S.C.) Among many other provisions, NSMIA amended the Securities Act of 1933 (codified at 15 U.S.C. §§ 77a et seq.) to pre-empt state registration and review of "covered securities." These provisions are now codified at 15 U.S.C. § 77r(b)(4). "Covered securities" was originally defined so as to include exemptions promulgated by the SEC pursuant to its authority under section 4(2) of the '33 Act. Preemption was controversial, and for many years there were few such exemptions, the most notable one being the then-current version of Rule 506 of Reg. D. For a description of this, see Jennifer J. Johnson, *Private Placements: A Regulatory Black Hole*, 35 DEL. J. CORP. L. 151 (2010); Jeffrey D. Chadwick, *Proving Preemption by Proving Exemption: The Quandary of the National Securities Market Improvement Act*, 43 U. RICH. L. REV. 765 (2009). To give an idea of how important issuers and their counsel viewed the ability to avoid application of state securities laws, under that regime "some 99% of the amounts of securities sold, approaching \$1 trillion annually," relied on that single exemption. Manning Gilbert Warren III, *The Role of the States in the Regulation of Private Placements*, 102 KY. L. REV. 971, 982 (2014). The JOBS Act, however, amended the definition of "covered" security to specifically apply to shares issued in compliance with Reg. CF. See 15 U.S.C. § 77d(6).

21. In March of 2018, the U.S. Small Business Administration (SBA) issued a report reviewing equity crowdfunding under Reg. CF. Lindsay M. Abate, *One Year of Equity Crowdfunding: Initial Market Developments and Trends*, U.S. SMALL BUS. ADMIN., OFF. OF ADVOC. (Mar. 29, 2018), https://cdn.crowdfundinsider.com/wp-content/uploads/2018/03/SBA-Crowdfunding_Issue_Brief_2018.pdf [<https://perma.cc/M34D-RQE4>]. "The report is of the opinion that the SEC may want to consider whether certain aspects of the regulatory scheme are too complex or costly for small businesses to navigate and comply with. It must be noted that everyone engaged with the space will be in agreement with this statement." JD Alois, *US Small Business Administration Publishes Report on Small Business Equity Crowdfunding under Reg CF*, CROWDFUND INSIDER (Mar. 29, 2018), <https://www.crowdfundinsider.com/2018/03/131207-us-small-business-administration-publishes-report-on-small-business-equity-crowdfunding-under-reg-cf/> (last visited Feb. 02, 2019) [<https://perma.cc/GD76-22AT>].

22. Christopher G. Froelich, *Let's Finally Fix Crowdfunding!*, VC EXPERTS BLOG (Apr. 18, 2017), <https://blog.vcexperts.com/2017/04/18/lets-finally-fix-crowdfunding/> (last visited Feb. 02, 2019) [<https://perma.cc/Z37B-WMCG>]. These burdens range from the requirement that firms raising more than \$535,000 prepare their financial statements in accordance with GAAP (generally accepted accounting principles), file a Form C (which is sufficiently complicated that it is likely to require expensive legal review), and limits on solicitation or advertising.

the question of what alternatives exist for businesses seeking to raise funds in a lawful manner.²³

Obviously, there are other federal exemptions that might come into play.²⁴ However, in Arkansas there is another alternative that deserves consideration: the Arkansas crowdfunding option.²⁵

The Arkansas Approach

In 2017, State Representative Lundstrum introduced “An Act to Amend Various State Securities Laws; to Regulate Securities Transactions; and for Other Purposes.”²⁶ As a result of this act, which was adopted on March 27, 2017,²⁷ the Arkansas Securities Laws were amended effective August 1, 2017, so as to provide a state level crowdfunding option.²⁸ While not perfect, the Arkansas version of crowdfunding may provide a viable alternative where compliance with Reg. CF at the federal level is impractical.²⁹

Among other provisions, the Act added a new exempt transaction authorizing crowdfunding in the state.³⁰ This exemption is available only if a particular offering is exempt from the federal securities law by virtual of section 3(a) (11) of the

23. Certainly there are reports of non-compliant Reg. CF offerings. One source has suggested that about 35% of Reg. CF issuers “are conducting, or have conducted, offerings with non-compliant financial statements.” Andrew Stephenson, *Compliance with Reg CF: Financial statements under Rule 201*, CROWDCHECK BLOG (Sept. 12, 2016), <https://www.crowdcheck.com/blog/compliance-reg-cf-financial-statements-under-rule-201> (last visited Feb. 02, 2019) [<https://perma.cc/Z2R5-JKNJ>]. Presumably, other regulatory requirements may also have been ignored. This article, of course, does not advocate non-compliant fundraising.

24. Transactional exemptions from registration under federal law are found in section 4 of the Securities Act of 1933 (the ‘33 Act), which is codified at 15 U.S.C. § 77d (2012). These exemptions range from non-issuer transactions, non-public offerings, offerings solely to accredited investors, to limited offerings, as well as authorizing crowdfunding sales under section 4(a)(6), codified at 15 U.S.C. § 77d(a)(6) (2012). Many of these exemptions are expanded or explained through SEC Regulations, such as Reg. A (codified at 17 C.F.R. §§ 230.251 - 230.346 (2018)) and Reg. D (codified at 17 C.F.R. §§ 230.500 - 230.508 (2018)), to name two of the most widely discussed.

25. ARK. CODE ANN. § 23-42-504(a)(12) (2017).

26. H.B. 1800, 91st Gen. Assemb., Reg. Sess. (Ark. 2017).

27. H.B. 1800, 91st Gen. Assemb., Reg. Sess. (Ark. 2017).

28. ARK. CODE ANN. § 23-42-504(a)(12) (2017).

29. See ARK. CODE ANN. § 23-42-504(a)(12) (2017).

30. ARK. CODE ANN. § 23-42-504(a)(12) (2017).

Securities Act of 1933 (the ‘33 Act)³¹ and its corresponding safe harbor, Rule 147,³² or by virtue of Rule 147A³³ promulgated pursuant to the authority granted in section 28 of the ‘33 Act,³⁴ as those provisions existed on January 1, 2017.³⁵ All of these provisions deal with intrastate offerings,³⁶ which require that the issuer be located (and for Rule 147 organized) in the state where an intrastate offering is to occur,³⁷ that the issuer be doing business there,³⁸ and that all purchasers (and for Rule 147 all offerees as well) reside in that state.³⁹ As the SEC has explained, “Rule 147A is substantially identical to Rule 147” except that it:

allows offers to be accessible to out-of-state residents, so long [as] sales are only made to in-state residents and permits a company to be incorporated or organized out-of-state, so long as the company has its “principal place of business” in-state and satisfies at least one “doing business” requirement that demonstrates the in-state nature of the company’s business.⁴⁰

In essence, Rules 147 and 147A provide a safe harbor demonstrating compliance with the statutory exemption,⁴¹ so that satisfying the terms of the Rules is sufficient but not required to invoke the federal exemption.⁴² To qualify for the Arkansas state crowdfunding exemption, the issuer must not only comply with the section but also the applicable intrastate safe harbor or rule.⁴³ Once this is done, however, an issuer may be able to proceed with

31. 15 U.S.C. § 77c(a)(11) (2012).

32. Rule 147 is codified at 17 C.F.R. § 230.147 (2018).

33. Rule 147A is codified at 17 C.F.R. § 230.147A (2018).

34. The Arkansas Code mistakenly refers to this as section 28 of the “Securities Exchange Act of 1933,” but that is clearly a typographical error. See ARK. CODE ANN. § 23-42-504(a)(12)(A) (2017), also noting that the section 28 to which it refers is codified at 15 U.S.C. § 77z-3 (which is part of the ‘33 Act).

35. ARK. CODE ANN. § 23-42-504(a)(12)(A) (2017).

36. ARK. CODE ANN. § 23-42-504(a)(12)(A) (2017).

37. ARK. CODE ANN. § 23-42-504(a)(12)(A) (2017).

38. ARK. CODE ANN. § 23-42-504(a)(12)(A) (2017).

39. ARK. CODE ANN. § 23-42-504(a)(12)(A) (2017).

40. Intrastate Offerings, U.S. SEC. EXCH. COMM’N,

<https://www.sec.gov/smallbusiness/exemptofferings/intrastateofferings> (last visited Feb. 02, 2019) [<https://perma.cc/U96K-X2ZK>].

41. 17 C.F.R. § 230.147 (2018); 17 C.F.R. § 230.147A (2018).

42. 17 C.F.R. § 230.147 (2018); 17 C.F.R. § 230.147A (2018).

43. This requirement is codified at ARK. CODE ANN. § 23-42-504(a)(12)(A) (2017).

crowdfunding in Arkansas even if a federal Reg. CF offering would have been too cumbersome or expensive.⁴⁴

Once it is clear that an offering is intrastate in nature under these rules, an Arkansas issuer, offering or selling solely to Arkansas residents, may raise up to \$1,000,000, less all amounts received from the sale of securities within six months after completing the offering.⁴⁵ Unlike federal law, which imposes a sliding scale on the amount that any one investor may contribute,⁴⁶ there is a straight-forward \$5,000 cap on investment from any single, unaccredited purchaser.⁴⁷ The state statute, as amended, does not include a maximum limit on the amount that may be contributed if the purchaser is accredited.⁴⁸ The issuer must reasonably believe that purchasers are buying for investment and not resale,⁴⁹ but sales need not occur through a registered broker-dealer or funding portal such as those required in the federal crowdfunding provisions.⁵⁰ Instead, if the issuer intends to pay commissions or remuneration for any person's participation in the offering, such person must be a registered broker-dealer under Arkansas law.⁵¹ The only other requirement included in the Arkansas statute is the requirement that the issuer must file a proof of exemption with the commissioner⁵² along with a required \$100 fee.⁵³ There is, however, a specific notation that the state

44. For a more detailed consideration of the federal intrastate offering exemption requirements, see Thomas Lee Hazen, *The Exemption for Purely Intrastate Offerings—The Statutory Exemption—Section 3(a)(11)*, in 1 LAW SEC. REG. § 4:25, Westlaw (database updated May 2018) and Robert J. Haft & Peter M. Fass, *Transactional Exemptions From Registration Requirements of the 1933 Act*, 1 TAX ADV. SEC. HANDBOOK § 3:3, Westlaw (database updated July 2018).

45. ARK. CODE ANN. § 23-42-504(a)(12)(B) (2017).

46. See 17 C.F.R. § 227.100(a)(2) (2018).

47. ARK. CODE ANN. § 23-42-504(a)(12)(C) (2017).

48. ARK. CODE ANN. § 23-42-504(a)(12)(C) (2017). This provision specifically cross-references the definition of accredited investor found in Rule 501 of Reg. D, codified at 17 C.F.R. § 230.501 (2018). The definition is fixed “as it existed on January 1, 2017” for purposes of Arkansas law. ARK. CODE ANN. § 23-42-504(a)(12)(C) (2017).

49. ARK. CODE ANN. § 23-42-504(a)(12)(D) (2017).

50. The federal requirement is found in Reg. CF at 17 C.F.R. § 227.100(a)(3).

51. ARK. CODE ANN. § 23-42-504(a)(12)(E) (2017).

52. The proof of exemption requirement for the Arkansas crowdfunding exemption as codified at ARK. CODE ANN. § 23-42-504(a)(12) appears in Rule 504.01(a)(12)(B)(i) of the Rules of the Arkansas Securities Commissioner. 214-00-005 ARK. CODE R. § 214.00.1-504.01(a)(12)(B)(i) (2018). Rule 506.01 also conditions the granting of an exemption from registration upon the filing of the proof of exemption before any offers can be accepted or contractual obligations entered into. 214-00-005 ARK. CODE R. § 214.00.1-506.01 (2018).

53. ARK. CODE ANN. § 23-42-504(a)(12)(G) (2017).

securities commissioner “may by rule or order, as to any security or transaction or any type of security or transaction, withdraw or further condition the exemption.”⁵⁴

In fact, the Arkansas Securities Department has added requirements to the Arkansas crowdfunding exemption,⁵⁵ all of which appear to be focused on increasing the level of protection for investors and potential investors or to improve the ability of the state to oversee the offerings.⁵⁶ The first additional requirement imposes an obligation on the issuer to escrow all funds received until the aggregate capital received at least equals the minimum target offering amount.⁵⁷ The second addition to the statute requires the issuer to provide the state commissioner with a wide range of written information,⁵⁸ including the proof of exemption,⁵⁹ any general advertising or sales material used in connection with the offering,⁶⁰ the offering documents that will be provided to each prospective purchaser,⁶¹ and a “copy of the

54. ARK. CODE ANN. § 23-42-504(a)(12)(F) (2017).

55. See 214-00-005 ARK. CODE R. § 214.00.1-504.01(a)(12) (2018).

56. 214-00-005 ARK. CODE R. § 214.00.1-504.01(a)(12)(A) (2018).

57. The actual language of the regulation is that the issuer “shall provide the Commissioner with a copy of the . . . escrow agreement with a bank, or depository institution authorized to do business in Arkansas where all funds received from investors shall be deposited until the aggregate capital raised from all purchasers is equal to or greater than the minimum target offering amount specified in the disclosure statement as necessary to implement the business plan. Investors shall receive a return of all their subscription funds if the target offering amount is not raised by the time stated in the disclosure statement. All the funds received from investors shall be used in accordance with all representations made to investors.” 214-00-005 ARK. CODE R. § 214.00.1-504.01(a)(12)(A) (2018).

58. 214-00-005 ARK. CODE R. § 214.00.1-504.01(a)(12)(B) (2018).

59. 214-00-005 ARK. CODE R. § 214.00.1-504.01(a)(12)(B)(i) (2018).

60. 214-00-005 ARK. CODE R. § 214.00.1-504.01(a)(12)(B)(ii) (2018).

61. The regulations include a list of minimum information that must be included in the offering documents provided to prospective purchasers. 214-00-005 ARK. CODE R. § 214.00.1-504(a)(12)(B)(iii) (2018). The required disclosures include basic information about the issuer and its management and business, a description of the purpose and intended use of proceeds, the target amount to be raised, a description of pending legal proceedings, and required disclosures relating to limits on resale (which must track federal limits as provided in SEC Rule 144(e) – (f)). 214-00-005 ARK. CODE R. § 214.00.1-504(a)(12)(B)(iii) (2018). It also includes certain financial documentation, including income tax returns, financial statements certified by the issuer’s principal executive officer, and audited financials for the past three years if they have already been prepared. 214-00-005 ARK. CODE R. § 214.00.1-504(a)(12)(B)(iii)(g) (2018). It is notable that the mandatory financial statements do not need to be prepared in accordance with GAAP, as they would under the federal Reg. CF. Compare the Arkansas requirements under Rule 504.01(a)(12)(B)(iii)(g) with 17 C.F.R. § 227.201(t) (2018), *Instruction 3*, which specifies that the required financial statements “must be prepared in accordance with U.S. generally accepted accounting principles and include

restrictive legend . . . evidencing that the securities have not been registered and setting forth the limitations on resale contained in SEC Rule 147(e). . . .⁶²

The Distinctions

The differences between the federal crowdfunding exemption under Reg. CF and Arkansas crowdfunding are significant and critical to an understanding and evaluation of funding options.⁶³ While the maximum total amounts that can be raised are only marginally different,⁶⁴ the Arkansas rules have much simpler limitations on the amount that may be contributed by individual investors.⁶⁵ Rather than having to inquire as to other offerings in which an investor may have participated and each investor's income and assets, there is a simple \$5,000 cap for any unaccredited investor.⁶⁶ Accredited investors in an Arkansas crowdfunding sale are not subject to any maximum investment.⁶⁷

Another burden imposed by the federal process is the mandate that a Reg. CF offering take place exclusively through the services of a registered broker-dealer or a registered funding portal.⁶⁸ There is no such requirement under Arkansas law.⁶⁹ This

balance sheets, statements of comprehensive income, statements of cash flows, statements of changes in stockholders' equity and notes to the financial statements.”

62. 214-00-005 ARK. CODE R. § 214.00.1-504(a)(12)(B)(iv) (2018). Rule 147(e) provides that for six months after purchase, the security in question may be resold “only to persons resident within the state or territory in which the issuer was resident, as determined pursuant to paragraph (c) of this section, at the time of the sale of the security by the issuer.” 17 C.F.R. § 230.147(e) (2018). This might actually be a slight typographical error in the Arkansas regulation, since the actual restrictive legend appears in the following subsection of the federal regulation. *See* 17 C.F.R. § 230.147(f) (2018).

63. *See infra* Table 1 (comparing Arkansas' crowdfunding exemption against Reg. CF).

64. The maximum that can be raised under Reg. CF is \$1,070,000 (17 C.F.R. § 227.100(a)(1) (2018)), while the cap under Arkansas law is \$1,000,000 (ARK. CODE ANN. § 23-43-504(a)(12)(B) (2017)).

65. *See* ARK. CODE ANN. § 23-42-504(a)(12)(C) (2017) (capping individual investor contributions at \$5,000).

66. *Compare* 17 C.F.R. § 227.100(a)(2) (invoking a sliding scale), *with* ARK. CODE ANN. § 23-42-504(a)(12)(C) (2017) (a flat rate).

67. ARK. CODE ANN. § 23-42-504(a)(12)(C) (2017). Presumably, the issuer would use something like an investor qualification statement in order to have a reasonable belief that the investor is, in fact, accredited. *See* ARK. CODE ANN. § 23-42-504(a)(12)(D) (2017).

68. 17 C.F.R. § 227.100(a)(3) (2018).

69. *See generally* ARK. CODE ANN. § 23-43-504 (2017) (mandating pre-transaction requirements in certain circumstances, but not mandating the use of a registered intermediary).

difference can potentially save an issuer a considerable amount in fees and commissions,⁷⁰ although it should be noted that if an issuer selling securities in compliance with the Arkansas crowdfunding rules does wish to compensate persons for their selling efforts, those persons must be registered broker-dealers.⁷¹

Another potentially significant difference relates to the complexity of the general disclosures required.⁷² Reg. CF offerings require the issuer to prepare an offering document,⁷³ which includes a wide range of required information.⁷⁴ While some information is also required under the Arkansas crowdfunding exemption,⁷⁵ it is considerably less extensive.⁷⁶ Disclosure obligations under the state requirements are such that it should be possible to prepare most of the information either with no or minimal legal assistance,⁷⁷ while navigating the disclosure requirements imposed by Reg. CF will likely require experienced (and expensive) securities counsel.⁷⁸

The financial disclosures in particular are likely to be far more burdensome under Reg. CF as compared to the state requirements. Reg. CF requires financial statements that must be prepared in accordance with specific accounting principles.⁷⁹ If

70. See Bevilacqua, *supra* note 8.

71. ARK. CODE ANN. § 23-43-504(a)(12)(E) (2017); 214-00-005 ARK. CODE R. § 214.00.1-504(a)(12)(C) (2018).

72. See *infra* Table 1, pp. 18-22 (detailing the differences in required disclosures).

73. Issuers relying on Reg. CF must provide the SEC, and all prospective purchasers, Form C. See *supra* note 13.

74. See sources cited *supra* note 13. See also *infra* Table 1 (providing a partial list of the required information).

75. See 214-00-005 ARK. CODE R. § 214.00.1-504(a)(12)(B)(iii) (2018).

76. See *infra* Table 1 (providing a side-by-side comparison of information required).

77. See 214-00-005 ARK. CODE R. § 214.00.1-504(a)(12)(B)(iii) (2018) (legally required disclosures are simple and do not mandate disclosure of capital structure or detailed financials).

78. One source has estimated that total fees for equity crowdfunding under Reg. CF could be \$60,000. Bevilacqua, *supra* note 8. This would include preparing the Form C offering statement, reviewing materials for the funding portal, and preparation of ancillary documentation. Much of that can be minimized if the extensive disclosure regime imposed by Reg. CF is avoided. As the same source notes, “[t]he Form C Offering Statement, which is very similar in size to a standard private placement memorandum, is responsible for most of the legal costs.” Bevilacqua, *supra* note 8.

79. See 17 C.F.R. § 227.201(t) (2018). For offerings up to \$107,000, Instruction 3 to paragraph (t) says that “[t]he financial statements must be prepared in accordance with U.S. generally accepted accounting principles and include balance sheets, statements of comprehensive income, statements of cash flows, statements of changes in stockholders’ equity and notes to the financial statements. If the financial statements are not audited, they must be labeled as ‘unaudited.’” 17 C.F.R. § 227.201(t) (2018).

more than \$107,000 is being raised, the issuer must retain outside public accountants.⁸⁰ Both of these requirements can be expensive and burdensome for smaller issuers, and there is no corresponding requirement that these steps be taken if the Arkansas exemption is utilized.⁸¹

The most significant burden that can be avoided under the Arkansas process, however, is likely to occur after the crowdfunding sale is completed.⁸² Reg. CF requires a company that has completed a crowdfunding offering to make extensive annual reports.⁸³ Assembling the contents of these reports may be quite expensive and burdensome for a new or emerging enterprise.⁸⁴ While it is possible that the obligation to make such annual disclosures may eventually be terminated, the circumstances under which an issuer can cease the ongoing reporting are limited,⁸⁵ and at a minimum include at least one annual follow-up report unless the business liquidates before the

80. For offerings involving more than \$107,000 the statements must be reviewed, and they must be audited if more than \$535,000 is to be raised. 17 C.F.R. § 227.201(t) (2018). If the statements are reviewed, the review “shall be conducted in accordance with the Statements on Standards for Accounting and Review Services issued by the Accounting and Review Services Committee of the American Institute of Certified Public Accountants. A signed review report must accompany the reviewed financial statements, and an issuer must notify the public accountant of the issuer’s intended use of the review report in the offering. An issuer will not be in compliance with the requirement to provide reviewed financial statements if the review report includes modifications.” 17 C.F.R. § 227.201(t) (2018), *Instruction 3*. If the statement is audited, it “shall be conducted in accordance with either auditing standards issued by the American Institute of Certified Public Accountants (referred to as U.S. Generally Accepted Auditing Standards) or the standards of the Public Company Accounting Oversight Board. A signed audit report must accompany audited financial statements, and an issuer must notify the public accountant of the issuer’s intended use of the audit report in the offering. An issuer will not be in compliance with the requirement to provide audited financial statements if the audit report includes a qualified opinion, an adverse opinion, or a disclaimer of opinion.” 17 C.F.R. § 227.201(t) (2018), *Instruction 9*. *Instruction 10* sets out independence standards for the accountant.

81. See 214-00-005 ARK. CODE R. § 214.00.1-504.01(a)(12)(B)(iii)(g) (2018).

82. See 214-00-005 ARK. CODE R. § 214.00.1-504.01(a)(12)(B)(iii)(g) (2018).

83. Following a Reg. CF offering, substantial annual reports are required, which must include certified or independently reviewed or audited financial statements, and a substantial portion of the information required in the original offering documents. 17 C.F.R. § 227.203(b) (2018).

84. One source has suggested annual reporting costs could be between \$2,000 to \$5,000, exclusive of accounting fees which might range between \$3,000 and \$7,500 depending on the complexity of the company’s financial situation. Bevilacqua, *supra* note 8.

85. See 17 C.F.R. § 227.202(b) (2018) for requirements to terminate ongoing reporting.

time the report would be due.⁸⁶ While an issuer relying on the Arkansas crowdfunding exemption must make certain information available to purchasers free of charge on a quarterly basis,⁸⁷ the required information is relatively minimal.⁸⁸

There are, of course, a few requirements that are imposed under state law that have no corresponding burden under federal law.⁸⁹ Most of these relate to the requirement that the offering be exempt under federal law as an exclusively intrastate offering.⁹⁰ Thus, for example, an Arkansas crowdfunding sale must be restricted to Arkansas residents,⁹¹ and the issuer must have its principal business here.⁹² For the first six months after purchase, resales are limited to other Arkansas residents.⁹³ In addition to the requirements that relate to the intrastate nature of the offering, Arkansas imposes an escrow requirement that is not matched by federal law.⁹⁴ These costs, however, seem substantially lower than the burdens of compliance with the terms of federal Reg. CF.⁹⁵

Perhaps the clearest way of demonstrating the distinction between the federal Reg. CF and Arkansas crowdfunding is to consider a side-by-side comparison of the requirements. The following table sets out, in abbreviated form, those differences. Where there are multiple options for compliance, the least burdensome are listed,⁹⁶ and references to the Arkansas Rules mean the Rules of the Arkansas Securities Commissioner.

86. The available ways in which the ongoing reporting obligation may end include going public (which will then subject the issuer to additional ongoing reporting obligations under the Securities Exchange Act of 1934); by filing at least one report and then having fewer than 300 holders of record of securities; by filing at least three reports and having total assets that do not exceed \$10,000,000; if all securities issued in reliance on section 4(a)(6) of the '33 Act are reacquired or purchased; or the issuer liquidates. 17 C.F.R. § 227.202(b) (2018).

87. 214-00-005 ARK. CODE R. § 214.00.1-504.01(a)(12)(G) (2018).

88. Under 214-00-005 ARK. CODE R. § 214.00.1-504.01(a)(12)(G) (2018), the issuer must provide a quarterly report listing the compensation of officers, directors and control persons, and an analysis of the issuer's business operations and financial conditions.

89. *See* ARK. CODE. ANN. § 23-42-504(a)(12)(A)(i) (2017).

90. ARK. CODE. ANN. § 23-42-504(a)(12)(A)(i) (2017).

91. ARK. CODE. ANN. § 23-42-504(a)(12)(A)(i) (2017).

92. ARK. CODE. ANN. § 23-42-504(a)(12)(A)(i) (2017).

93. 17 C.F.R. § 230.147A(e) (2017).

94. 214-00-005 ARK. CODE R. § 214.00.1-504.01(a)(12)(A) (2018).

95. *See* 17 C.F.R. § 227.100 (2018).

96. The clearest of these relates to the requirements set out in the second and third rows relating to the Arkansas crowdfunding limitations on where the issuer must be located and doing business. The Arkansas crowdfunding exemption requires that the issuer must either satisfy the terms of section 3(a)(11) of the '33 Act (codified at 15 U.S.C. § 77c(a)(11))

Table 1: Side-by-side Comparison of Federal Reg. CF and Arkansas Crowdfunding

Requirement	Federal Reg. CF	Arkansas Crowdfunding
Limits on kind of issuer eligible for the exemption.	May not be a reporting company; an investment company; disqualified as a bad actor under 17 C.F.R. § 227.503(a) (2018); out of compliance for failing to provide required reports in the prior two years; or a company that has no business plan regarding the use of proceeds or whose only plan is to engage in merger/acquisition with an unidentified company. (17 C.F.R. § 227.100(b)(2)-(6) (2018)).	Essentially the same limitations as imposed by Reg. CF apply. (214-00-005 ARK. CODE R. § 214.00.1-504.01(a)(12)(D) (2018)).
Where must issuer be located and what that means.	Must be organized and subject to laws of a state, territory of the U.S., of the District of Columbia. (17 C.F.R. § 227.100(b)(1) (2018)).	Must be located in Arkansas, with its principal place of business in Arkansas (meaning activities must be primarily controlled by persons from in this state). (ARK. CODE ANN. § 23-42-504(a)(12)(A) (2017), incorporating the requirements of 17 C.F.R. § 230.147A(c)(1) (2018)).

and SEC Rule 147 (codified at 17 C.F.R. § 230.147), or section 28 of the Securities Exchange Act of 1933 [sic] (this is undoubtedly supposed be a reference to the '33 Act) (codified at 15 U.S.C. § 77z-3) and SEC Rule 147A (codified at 17 C.F.R. § 230.147A), all as they existed on January 1, 2017. ARK. CODE ANN. § 23-42-504(a)(12)(A)(i) (2017). In each case in the table, Rule 147A is substantially less burdensome, and therefore those are the minimum requirements included in the table.

Any requirement for doing business in a particular state.	There are no requirements as to how many states in which the issuer operates.	As consolidated with subsidiaries, at least 80% of income must be derived from Arkansas operations, or 80% of assets must be located in state, or the intent must be to use at least 80% of proceeds in Arkansas, or most of the issuer's employees must be based in Arkansas. (ARK. CODE ANN. § 23-42-504(a)(12)(A) (2017), incorporating the requirements of 17 C.F.R. § 230.147A(c)(2) (2018)).
To whom may the issuer sell.	No limits (other than as to amount that may be sold to each).	Only to Arkansas residents. (ARK. CODE ANN. § 23-42-504(a)(12) (2017), incorporating the requirements of 17 C.F.R. § 230.147A(d) (2018)).
Total amount that may be raised.	\$1,070,000. (17 C.F.R. § 227.100(a)(1) (2018)).	\$1,000,000. (ARK. CODE ANN. § 23-42-504(a)(12)(B) (2017)).
Maximum amount raised from any unaccredited investor.	The greater of \$2,200 or 5% of the lesser of the investor's annual income or net worth if either the investor's annual income or net worth is less than \$107,000; or 10% of the lesser of such amounts if both exceed \$107,000, REDUCED by amounts paid to all other issuers in the preceding 12 months. (17 C.F.R. § 227.100(a)(2) (2018)).	\$5,000. (ARK. CODE ANN. § 23-42-504(a)(12)(C) (2017)).

Maximum amount raised from an accredited investor.	Maximum is \$107,000 (also reduced for amounts paid to all other issuers in the prior 12 months) regardless of wealth (17 C.F.R. § 227.100(a)(2)(ii) (2018)).	No limit. (ARK. CODE ANN. § 23-42-504(a)(12)(C) (2017)).
Intermediary required?	Yes, issuer may only sell through a regulated broker-dealer or funding portal, and the transaction must be conducted exclusively through that platform. (17 C.F.R. § 227.100(a)(3) (2018)). Disclosure to and about the intermediary is also mandated. (17 C.F.R. § 227.201(n)(o) (2018)).	No.
Limits on commission (or other payments).	No limits on issuer's ability to pay commissions.	No commissions are allowed unless the issuer uses and pays only licensed broker-dealers (ARK. CODE ANN. § 23-42-504(a)(12)(E) (2017) & 214-00-005 ARK. CODE R. § 214.00.1-504.01(a)(12)(C) (2018)).
Advance filing required?	Yes, Form C (the offering statement) must be filed with the SEC prior to any offer or sale (17 C.F.R. § 227.203(a)(1) (2018)), progress updates are required (17 C.F.R. § 227.203(a)(3)(i) (2018)), and all information provided to investors and the relevant intermediary must also be filed with SEC. (17 C.F.R. § 227.201 (2018)).	Yes, proof of exemption plus all advertising materials, and all information provided to prospective purchasers must be filed with Ar Securities Commission at least 10 days before any offer or sale. (214-00-005 ARK. CODE R. § 214.00.1-504.01(a)(12)(B) (2018)).

Are disclosures about issuer required?	Yes, its name and legal status must be disclosed (17 C.F.R. § 227.201(d) (2018)) as well the nature of its business and number of employees. (17 C.F.R. § 227.201(d)(e) (2018)).	Yes, name, legal status, physical and website address. (214-00-005 ARK. CODE R. § 214.00.1-504.01(a)(12)(B)(iii)(a) (2018)).
Are disclosures about management required?	Yes, directors' and officers' names, positions, length of service with the issuer, their principal occupation for at least the prior three years as well as the name and business of any organization where such employment occurred. (17 C.F.R. § 227.201(b) (2018)).	Yes, names of directors, officers and control persons. (214-00-005 ARK. CODE R. § 214.00.1-504.01(a)(12)(B)(iii)(b) (2018)).
Are disclosures about ownership and identification significant owners required?	Yes, the ownership and capital structure of the issuer must be disclosed (17 C.F.R. § 227.201(m) (2018)), along with the name of every person who (no more than 120 days before disclosure) owned at least 20% of issuer's voting power. (17 C.F.R. § 227.201(c) (2018)).	No.
Disclosure of risk factors required?	Yes. (17 C.F.R. § 227.201(f) (2018)).	Not specifically.
Disclosure of legal proceedings required?	Only to the extent that disclosure is required to make other disclosures "not misleading" in a material way. (17 C.F.R. § 227.201(y) (2018)).	Yes. (214-00-005 ARK. CODE R. § 214.00.1-504.01(a)(12)(B)(iii)(h) (2018)).

Disclosure of target amount and timetable required?	Yes, along with the maximum amount that will be accepted. (17 C.F.R. § 227.201(g) (2018)).	Yes, the target amount and deadline. (214-00-005 ARK. CODE R. § 214.00.1-504.01(a)(12)(B)(iii)(e) (2018)).
Disclosure of use of proceeds required?	Yes. (17 C.F.R. § 227.201(i) (2018)).	Yes, the stated purpose and intended use of the proceeds of the offering sought by the issuer, including all compensation paid to any officer, director, or control person. (214-00-005 ARK. CODE R. § 214.00.1-504.01(a)(12)(B)(iii)(d) (2018)).
Do investors have a right to withdraw amounts sent in?	Yes, up to 48 hours before deadline that must be announced in offering materials, or if target is reached earlier they have five days in which they may change their mind. (17 C.F.R. § 227.201(j) (2018)).	Not unless the target amount is not reached by the deadline. (214-00-005 ARK. CODE R. § 214.00.1-504.01(a)(12)(A) (2018), dealing with the terms of the escrow).
Must the issuer explain how its securities are valued?	Yes. (17 C.F.R. § 227.201(l) & (m)(4) (2018)).	Not specifically mandated.
Does issuer need to disclose prior offerings?	Yes, for any exempt offerings in the prior three years specific information must be disclosed. (17 C.F.R. § 227.201(q) (2018))	No.

Do specific transactions need to be disclosed?	Yes, since the last fiscal year, and for any proposed transaction, any transaction exceeding 5% of the capital being raised along with any other amounts raised in similar exempt sales in the prior 12 month, if there is any potential conflict of interest as detailed in the regulation. (17 C.F.R. § 227.201(r) (2018)). Material indebtedness of the issuer must also be disclosed. (17 C.F.R. § 227.201(p) (2018)).	No.
Must the issuer include a general discussion of financial information?	Yes, including, “to the extent material, liquidity, capital resources and historical results of operations.” (17 C.F.R. § 227.201(s) (2018)).	Not specifically required.

<p>What other financial information must be disclosed?</p>	<p>For offerings up to \$107,000, total income, taxable income, and total tax reported on the issuer's tax returns for the prior two years, plus financial statements that must be prepared in accordance with GAAP. (17 C.F.R. § 227.201(t)(1) (2018), and <i>Instructions</i> 3 & 4 to paragraph (t)). For offerings over \$107,000 but no more than \$535,000, financial statements prepared in accordance with GAAP and reviewed or audited by an independent public accountant. (17 C.F.R. § 227.201(t)(2) (2018), and <i>Instructions</i> 3,4,8, 9 & 10 to paragraph (t)). If more than \$535,000 is being raised, the financial statements must be audited by an independent public accountant. (17 C.F.R. § 227.201(t)(3) (2018), and <i>Instructions</i> 3,4,8, 9 & 10 to paragraph (t)).</p>	<p>Most recent year's tax return, financial statements, and audited financial statements for the prior three years but only if the issuer has had them prepared. (214-00-005 ARK. CODE R. § 214.00.1-504.01(a)(12)(B)(iii)(g) (2018)).</p>
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Does the Issuer's chief executive need to certify the financial statements provided to investors?	Yes, unless the statements are reviewed or audited by an independent public accountant. (17 C.F.R. § 227.201(i)(1) (2018); see also <i>Instructions</i> 8, 9 and 10 for requirements that must be met in order to avoid the necessity of such certification.) Note that for any offering involving more than \$107,000 the certification is not necessary because the statements <u>must</u> be at least reviewed by an independent public accountant.	Yes, they must be certified as true and complete in all material respects. (214-00-005 ARK. CODE R. § 214.00.1-504.01(a)(12)(B)(iii)(g)(2) (2018)).
Are there on-going reporting required following a crowd-funding sale?	Following a Reg. CF offering, substantial annual reports are required, which must include certified or independently reviewed or audited financial statements, along with a substantial portion of the information required in the original offering documents (17 C.F.R. § 227.203(b) (2018)) until certain requirements are met and the purchasers are notified that annual reporting will cease. (See 17 C.F.R. § 227.202(b) (2018) for requirements to terminate ongoing reporting).	Yes, the issuer is to provide free of charge a quarterly report setting out the compensation of officers, directors and control persons, and an analysis of the issuer's business operations and financial conditions. (214-00-005 ARK. CODE R. § 214.00.1-504.01(a)(12)(G) (2018)).
escrow required	No, but there are withdrawal rights that the issuer must provide to all persons who pay in funds prior to closing of the offering. (17 C.F.R. § 227.201(j) (2018)).	Yes. (214-00-005 ARK. CODE R. § 214.00.1-504.01(a)(12)(A) (2018))

limits on resale	Yes, there is a one-year restriction on resale except to the issuer, an accredited investor, as part of a registered offering, or to a family member or trust controlled by or to benefit the purchaser or a family member, or in connection with the purchaser's death or similar circumstance. (17 C.F.R. § 227.501(a) (2018)).	Yes, "[t]he issuer should reasonably believe that all purchasers of securities are purchasing for investment and not for sale in connection with a distribution of the security," which means that resales will be restricted for a period of time. (ARK. CODE ANN. § 23-42-504(a)(12)(D) (2017)). In addition, resale is limited to Arkansas residents for six months. (17 C.F.R. § 230.147A(e) (2018)).
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This brief article does not fully flesh out the myriad requirements under either the federal or state crowdfunding exemption, but by setting out an overview of the two options, perhaps Arkansas practitioners will be more cognizant of the relatively new Arkansas crowdfunding exemption. Because it is likely to be less burdensome for issuers, it may provide a realistic alternative for clients seeking a relatively modest infusion of cash earlier in the life of a business enterprise. It is certainly less problematic than Reg. CF, which was a superb idea that has proven to be less than completely satisfactory in practice.