

## SEC Grants “Accredited Crowdfunding” Online Platforms Relief from Broker Dealer Registration

In two recent no action letters the SEC granted exemptive relief from broker dealer registration to crowdfunding sites on the basis that the platforms received carried interest rather than transaction base compensation. Although the SEC made it clear that the no-action letters were to be narrowly construed to the specific facts of each case, some commentators extrapolated that the letters indicate that the SEC is likely to take a similar position in regard to platforms seeking to help entrepreneurs raise capital from non-accredited investors under the JOBS Act’s crowdfunding provisions. According to securities attorney Simon Riveles, JOBS Act crowdfunding portals are unlikely, however, to be able to rely on the letters issued to FoundersClub, Inc. and AngelList LLC in so far as these JOBS Act crowdfunding platforms are unlikely to be compensated on the basis of carried interest.

While the structure and strategy employed by FoundersClub and AngelList differ in certain material respects, their central business models do not. Both companies have controlling entities that identify and vet promising early stage businesses. Once satisfied that a start-up is an attractive investment opportunity and is sound from a due diligence perspective the portals establish a wholly owned subsidiary to serve as the investment vehicle into the start-up. A set of pre-screened “accredited investors” may evaluate the start-up through the portals password protected web-platform and make an investment in the companies through the investment vehicle established for that purpose. The sponsor provides administrative services and investment advice to the investment vehicle including exercising any management rights the investment vehicle’s interest in the startup may possess.

The analysis set forth in the SEC letters focused on the following factors: (i) the investment opportunities both platforms offer are available only to “accredited” investors; (ii) the private securities offering comply with Rule 506 of Regulation D of the 1933 Securities Act (e.g. no general solicitation was employed to attract investors); (ii) a third party custodian handles investor securities, and; (iii) neither the sponsor of the platforms or its affiliates receive transaction based compensation. Rather, much like the manager of a venture capital or private equity fund, the sponsor is entitled to a portion of the profit made by each investor (“carried interest”).

The no-action letters in FoundersClub and AngelList do not represent a relaxation of the securities laws regarding private offerings and are not likely to have an impact on implementation of crowdfunding under the JOBS Act. Nevertheless, the letters remove an important potential impediment to the migration of venture capital investing to the web and are



likely to encourage additional players to get into the space – particularly in light of the lifting of the ban on general solicitation which will allow these platforms to market start up investing to the general public.