CAFE
Community Assistance Friends Enterprise

INFORMATIONAL SUMMARY

Raising Capital with Securities

The ability to secure ample funding is often the line between success and failure for many small businesses. Start-up capital is typically provided by the founders of the business and ownership shares or equity is divided at formation. Typically, the next round of fundraising is a friends and family round where investors are offered a portion of the company in exchange for their investment; however, this is where many small businesses run into serious legal issues. If a business sells equity (a portion of itself) to an investor, the business is issuing a security and must conform to Federal and State Securities and Exchange Commission Guidelines ("SEC"). Below are several exceptions and guidelines issued by the SEC that govern raising funds.

What Qualifies as Issuing a Security?

Any offer and sale of stock, bonds, ownership interests, or guaranteed percentage of businesses profits are considered "securities." All securities issued within the U.S. must either be registered with both the Federal and State SECs or fall within one of the exemptions from registration. Failure to properly register a security or file a notice of exemption can cause the issuer to incur financial or criminal penalties under antifraud provisions of the federal and state securities laws. However, registering a security with the SEC is an onerous and lengthy process that can incur significant legal expenses, so most small businesses seek to fall into one of the registration exemptions. Below is a description of some commonly used federal exemptions:

Regulation D Rule 504 (Seed Capital Exemption)

Eligibility	Benefits/Limits
• Allows for the offer and sale of up to $1,000,000 of securities in a 12-month period • Any business structure that allows for the sale of an ownership interest is eligible (sole proprietorships cannot issue securities) • Must file a Form D with the federal SEC and follow State registration / notification requirements	• Not subject to the SEC reporting and registration requirements • May not use general solicitation • Securities are restricted and may not be resold with registration

Note: there are several other Regulation D exemptions including 505 and 506 that offer higher upper limits on capital raises and come with higher regulatory and registration requirements, including requirements that investors must be "accredited" and/or "sophisticated." More information on securities can be found on the SEC website and Pennsylvania Department of Banking and Securities website.

Regulation Crowdfunding (Equity Crowdfunding)

Eligibility	Benefits/Limits
• Allows for the offer and sale of up to $1,070,000 of crowdfunded securities in a 12-month period • Any business structure that allows for the sale of an ownership interest is eligible (sole proprietorships cannot issue securities) • Must file a Form C with the federal SEC and follow State registration and notification requirements • Each securities offering must be issued through a single platform and issuing must be conducted through a platform or broker that is registered with the SEC	• Avoids restrictions on "sophisticated" or "Accredited" investors • Burden of investor compliance is placed on crowdfunding platform • The owner gets to set the terms of the offering

Note: More information on Regulation Crowdfunding can be found on the SEC website.

Issuing securities is complicated and heavily regulated; before issuing securities, you should consult with a securities attorney. The Pennsylvania Bar Associations and local County Bar Associations offer referrals.