# **Capital Raising in the U.S.:** An Analysis of the Market for Unregistered Securities Offerings, 2009-2017[1]

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## ABSTRACT

Capital formation through private placement of securities has increased substantially since the the 2008 global financial crisis. During recent years, amounts raised through unregistered securities offerings have outpaced the level of capital formation through registered securities offerings, and totaled more than $3.0 trillion during 2017. In this analysis, we provide insights into a large segment of the unregistered securities market[2]: offerings conducted in reliance on Regulation D of the Securities Act. Using information collected from Form D filings, this study provides a detailed examination of offering characteristics, including the types of issuers, investors, and financial intermediaries that participate in the offerings. As part of the examination, we analyze the new and amended exemptions created pursuant to the Jumpstart Our Business Startups Act of 2012 ("JOBS Act") – the new Rule 506(c) exemption which became effective in September 2013 and allows general solicitation and general advertising, changing almost 80 years of regulatory practice, the amended Regulation A which became effective June 19, 2015 and the new Regulation Crowdfunding that became effective May 16, 2016. We also provide some perspective on the state of competition and potential regulatory burden in alternate capital markets by analyzing the level of activity among the various registered and unregistered offering alternatives.

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This study was prepared for Chyhe Becker, Acting Director of DERA and Acting Chief Economist, and is a follow-up to a study conducted in 2015, which provided an analysis of capital raised through unregistered offerings for the period 2009-2014. See Scott Bauguess, Rachita Gullapalli and Vladimir Ivanov, Capital Raising in the U.S.: An Analysis of the Market for Unregistered Securities Offerings, 2009-2016 (October 2015) (the "2015 Unregistered Offerings Study"), available at: https://www.sec.gov/dera/staff-papers/white-papers/30oct15_white_unregistered_offering.html.
The information in this study may be particularly useful in assessing the potential need for current or future rulemaking activity. This analysis is not intended to inform the Commission about compliance with or enforcement of federal securities laws.
[2] As used throughout the study, the term "market" refers to capital markets in general, and, where discussed in the context of a specific rule, relates to the provisions of the relevant exemption or safe harbor.

## SUMMARY OF MAIN FINDINGS

- In 2017, there were 37,785 Regulation D offerings reported on Form D filings, accounting for more than $1.8 trillion raised in new capital.
- Issuers in non-financial industries[3] reported raising $105 billion during 2017. Among financial issuers, hedge funds reported raising $382 billion and private equity funds $582 billion, while financial issuers that are not pooled investment funds reported $72 billion during 2017 and $570 billion during the 2009-2017 period.
- Foreign issuers accounted for approximately 22% of the total amount reported sold during 2017. Most foreign issuers are firms from Canada, Cayman Islands, and United Kingdom.
- During 2009-2017, Rules 506(b) and 506(c) account for 99.9% of the amounts reported sold through Regulation D, including 93% of capital raised in offerings with maximum offer size of $1 million and 98% of capital raised below the amended Rule 504 offering limit threshold ($5 million), suggesting that issuers continue to value the preemption of state securities laws provided for offerings conducted pursuant to Rule 506. [4]
- Since the effectiveness of Rule 506(c) that eliminated the ban on general solicitation, only a small proportion (4%; $255 billion) of the capital raised in Regulation D offerings was raised in offerings conducted pursuant to Rule 506(c).
- Capital raised through Regulation D offerings continues to be positively correlated with public market performance, suggesting that capital formation in the unregistered market is pro-cyclical, i.e., the strength of the unregistered market is closely tied to the health of the public market and the overall economy.
- Consistent with the original intent of Regulation D to target the capital formation needs of small business, the median size of offerings by non-financial issuers is less than $1 million.
- Approximately 398,000 investors participated in Regulation D offerings during 2017. A large majority of these investors participated in offerings by non-financial issuers. Non-accredited investors were present in only 9% of Regulation D offerings.

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[3] All issuers that are not pooled investment funds (e.g., hedge funds, venture capital funds, and private equity funds) and that are not in the following Form D listed industries: commercial banking, insurance, investing, investment banking, and other banking & financial services. This group is primarily comprised of operating firms.

[4] Regulation D was amended in October 2016 to, among other things, increase the dollar amount offering threshold in Rule 504 from $1 million annually to $5 million annually and to eliminate Rule 505. *See* SEC Rel. No. 33-10238 (Oct. 26, 2016), available at: https://www.sec.gov/rules/final/2016/33-10238.pdf. The amendments to Rule 504 became effective on January 20, 2017, while the elimination of Rule 505 became effective on May 22, 2017.

## I. Introduction

Securities laws require that all offers and sales of securities be either registered with the Securities and Exchange Commission (SEC) under the Securities Act of 1933 or made in reliance upon an exemption from registration. When raising capital through the sale of securities to any potential investors in the public capital market (a "public" offering), the issuer must generally register the offer and sale of securities with the SEC, a process that is accompanied by extensive information production and subsequent reporting, unless an exemption from registration is available.[5] Alternatively, a company can raise capital by accessing the private capital markets through an unregistered ("private") offering in a transaction exempt from registration. In general, this path reduces an issuer's regulatory obligations, as compared to the obligations attendant to registered public offerings, thereby reducing issuance costs and the time required to raise new capital. This particularly benefits smaller firms, for whom accessing public capital markets may generally be too costly. However, because of these accommodations, private offering alternatives are generally subject to investor restrictions and/or offering limits. These investor protection provisions must be met to qualify for an exemption from registration.

The private offering market is governed by several exemptions from registration, including those under Sections 4(a)(2), 3(b) and 3(a)(11) of the Securities Act. For example, Section 3(b) is the exemptive authority for Rule 504 under Regulation D, as well as Regulation A that was amended, effective June 2015, pursuant to Title IV of the JOBS Act.[6] Other parts of the private market rely on "safe harbors": rules and regulations that set forth specific conditions that, if satisfied, ensure compliance with an exemption from registration. For example, issuers can use non-exclusive safe harbors such as Rule 506(b) of Regulation D, which is a safe harbor under Section 4(a)(2), Regulation S for offerings outside of the U.S., and Rule 144A for the resale of restricted securities to qualified institutional buyers (QIBs). A comparative analysis of the characteristics of these and other offering exemptions and safe harbors is provided in Appendix II. The Commission also recently adopted final rules that increased the maximum offer size under Rule 504 from $1 million to $5 million and repealed Rule 505 in light of its limited and declining usage.[7] These changes to Regulation D (amended Rule 504 and repeal of Rule 505) became effective in 2017.

The importance of private capital markets as a source of financing in the economy is underscored by the fact that less than 0.02% of the estimated 5.8 million employee-based firms

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[5] For example, an exception to the general rule exist in unregistered securities offerings conducted pursuant to Regulation A, an exemption from registration for securities offerings of up to $50 million annually.

[6] Among the changes in Regulation A is an increase in the amount of capital that can be raised (from $5 million to $50 million) and state securities law preemption for certain offerings.

[7] Exemptions to Facilitate Intrastate and Regional Securities Offerings, Release No. 33-10238 (October 26, 2016).

and 23.8 million non-employer firms in the U.S. are currently exchange listed firms.[8] Moreover, there has been a steady and significant decrease in the number of public reporting companies in the U.S., particularly since the dot com crash and implementation of the Sarbanes-Oxley Act.[9] During this period, private offerings of securities have contributed significantly to capital formation in the U.S. economy, particularly for small and emerging companies that are often considered to be the engine for creating new jobs,[10] driving innovation, and for accelerating economic growth. Hence, private capital markets provide an important financing alternative for companies that for various reasons forego financing in the public capital markets.

This study focuses on securities issuances by issuers that conduct unregistered offerings pursuant to Regulation D of the Securities Act. Currently, Regulation D is comprised of three rules: Rule 504, Rule 506(b) and Rule 506(c). [11] The analysis updates and extends previous work by SEC staff on this topic,[12] and includes a comprehensive look at the use and effect of the introduction of Rule 506(c) under Title II of the JOBS Act, which allows an issuer to generally solicit investors and generally advertise its offering. A critical component of our analysis is the data we rely on. The data used in the study, including how we compiled our sample, is described in detail in Appendix I. As the analysis below shows, Regulation D remains a widely used regulation for conducting unregistered offerings of securities. More than $1.8 trillion was reported as sold during 2017, the highest levels reported since Form D filings became machine readable in 2008.[13] This amount is larger than the amount of capital raised by public equity and debt offerings combined. And as indicated in the next Section, it is likely that the reported data on Regulation D offerings underestimates the actual amount raised through offerings where the issuer intended to rely on Regulation D. Most of the $1.8 trillion was reported raised through Rule 506(b), which prohibits general solicitation and general advertising, and limits investor participation to accredited investors and up to 35 sophisticated non-accredited[14],

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[8] Data is for 2014. *See* https://www.sba.gov/sites/default/files/advocacy/SB-FAQ-2017-WEB.pdf. *Also see*, There were 4,369 listed domestic companies in 2014. *See*, World Federation of Exchanges Database, World Bank. http://data.worldbank.org/indicator/CM.MKT.LDOM.NO?locations=US.

[9] *See* Doidge, C., A. Karolyi, and R. Stulz, *The U.S. Listing Gap*, The Journal of Financial Economics, Vol 123, Issue 3, March 2017.

[10] The United States Small Business Administration estimates show that small businesses accounted for 48% of U.S. employment during 2014, and contributed to creating 62% of all net new jobs during 1993-2016. *See* https://www.sba.gov/sites/default/files/advocacy/SB-FAQ-2017-WEB.pdf.

[11] See fn. 4 above.

[12] *See,* the 2015 Unregistered Offerings Study.

[13] Prior to 2008, filings were filed in paper making large scale extraction from tens of thousands of filings impractical.

[14] These are investors that do not meet the definition of an accredited investor provided under Rule 501 of Regulation D. Generally, accredited investors are institutions that have total assets of at-least $5 million or natural persons that have individual income of at least $200,000, joint income of at least $300,000, in each of the last two years and an expectation to reach the same income in the current year, or net-worth (excluding primary residence) of at-least $1 million. See Section IVb. for more information on investors in Regulation D offerings.

investors. Amounts reported raised under Rule 506(c) remain a small fraction of the total (4%) of the capital reported raised pursuant to Regulation D since the rule became effective on September 23, 2013, suggesting that most issuers of unregistered securities are not yet seeking investors through general solicitation and general advertising.

Among the other findings, the majority of the capital raised in the Regulation D market in 2017 was raised by pooled investment vehicles ($1,671 billion), while non-financial issuers raised $105 billion.[15] Regulation D offerings are very popular with small businesses: there have been more than 100,700 issuances by non-financial issuers since 2009, with a median offer size of less than $1 million. Unlike public offerings, only 20% of new Regulation D offerings since 2009 report using a financial intermediary. The average commission is 6%, but it varies significantly by the size of the offering and the type of the issuer involved.

The results of our analysis take into consideration several factors that may affect an issuer's choice of offering method for issuance of unregistered securities, such as preemption of state securities laws, ability to advertise, ability of non-accredited investors to participate, limits to the amount of capital that can be raised, geographical constraints, and level of required initial and ongoing disclosure to investors. These factors may affect both the level of burden (costs) incurred by an issuer to raise capital as well as the amount of protection available to investors, including, for instance, through additional oversight by state securities regulators.

Similarly, while Regulation D has been in existence since 1982, other private offering issuance methods are newer, such as those arising from the JOBS Act (e.g., the new Rule 506(c) effective since September 2013, the amended Regulation A effective since June 2015, the Regulation Crowdfunding since May 2016 and the amended Rule 147 and new Rule 147A for intrastate offerings that became effective April 2017). The last section in this study presents a comparative analysis of capital raising activity under Regulation D exemptions relative to Regulation A and Regulation Crowdfunding. Compared to Regulation A and Regulation Crowdfunding offerings, Regulation D offerings of similar offering sizes are much more numerous and raise significantly more capital. Additionally, very few Regulation Crowdfunding issuers have used the Regulation D market in the past, suggesting that Regulation Crowdfunding, at least based on data as of December 31, 2017, tends to bring new issuers to the private offering market rather than encouraging current issuers to switch between private offerings exemptions. A caveat is due, however, since we do not observe if these Regulation Crowdfunding issuers use other private offering exemptions for which we do not have data

[15] Pooled investment vehicles include hedge funds, private equity funds, venture capital funds, commodity pools, and a few other types of funds. In the paper we use the terms "pooled investment vehicles" and "funds" interchangeably. Non-financial issuers are defined as operating companies that are outside of the financial sector.

(e.g., Section 4(a)(2) offerings). As of December 31, 2017, approximately 61% of Regulation A issuers have undertaken private offerings[16], most of them in reliance on Section 4(a)(2) or Regulation D, suggesting that, at least based on the two and a half years of data since the changes in Regulation A became effective, most issuers in this market tend to switch between private offerings exemptions. Additionally, we do not have enough information to determine the extent to which some of these newer rules and the amendments to Regulation D that became effective in 2017 (amended Rule 504 and repeal of Rule 505) will affect the importance of Rule 506(b) and 506(c) of Regulation D or serve as alternatives to registered offerings.

The study is organized as follows. Section II provides an overview of the private offerings market. Section III provides an overview of capital formation in the market for Regulation D offerings. Section IV provides a detailed analysis of the characteristics of market participants in the Regulation D market. Section V compares Regulation D offerings and issuer characteristics to similar Regulation A and Regulation Crowdfunding offerings.

[16] See Anzhela Knyazeva, Regulation A+: What do we know so far? (November 2016), available at https://www.sec.gov/files/Knyazeva_RegulationA%20.pdf

## II. The size of the private offerings market

To estimate the total size of the private offerings market, we sum the total amount of securities sold using available data[17] for each of the main private offering exemptions during the period 2009-2017, including:

- Regulation D
- Rule 144A (resale of unregistered securities to QIBs)
- Regulation S (offshore component of 144A offerings)
- Regulation A offerings
- Regulation Crowdfunding offerings
- Other Section 4(a)(2) private offerings

Data for some of these exemptions is more readily available than for others. For example, because issuers relying on Section 4(a)(2) are not required to file any document with the Commission, offering information available in the commercial databases likely underestimates the amount of capital raised through this exemption. Similarly, the available data on Regulation D offerings could underestimate the true amount of capital raised through such offerings. While Rule 503 of Regulation D requires the filing of a notice on Form D no later than 15 days after the first sale of securities, the filing of a Form D is not a condition to claiming a Regulation D safe harbor or exemption, and it is possible that some issuers do not file Forms D for offerings relying on Regulation D.[18]

Figure 1 illustrates that the total capital raised annually in the private capital market is large both in absolute terms and when compared to the amounts raised in the public markets. In 2017, registered offerings accounted for $1.5 trillion of new capital compared to more than $3.0 trillion reported raised through all private offering channels. The amount raised by

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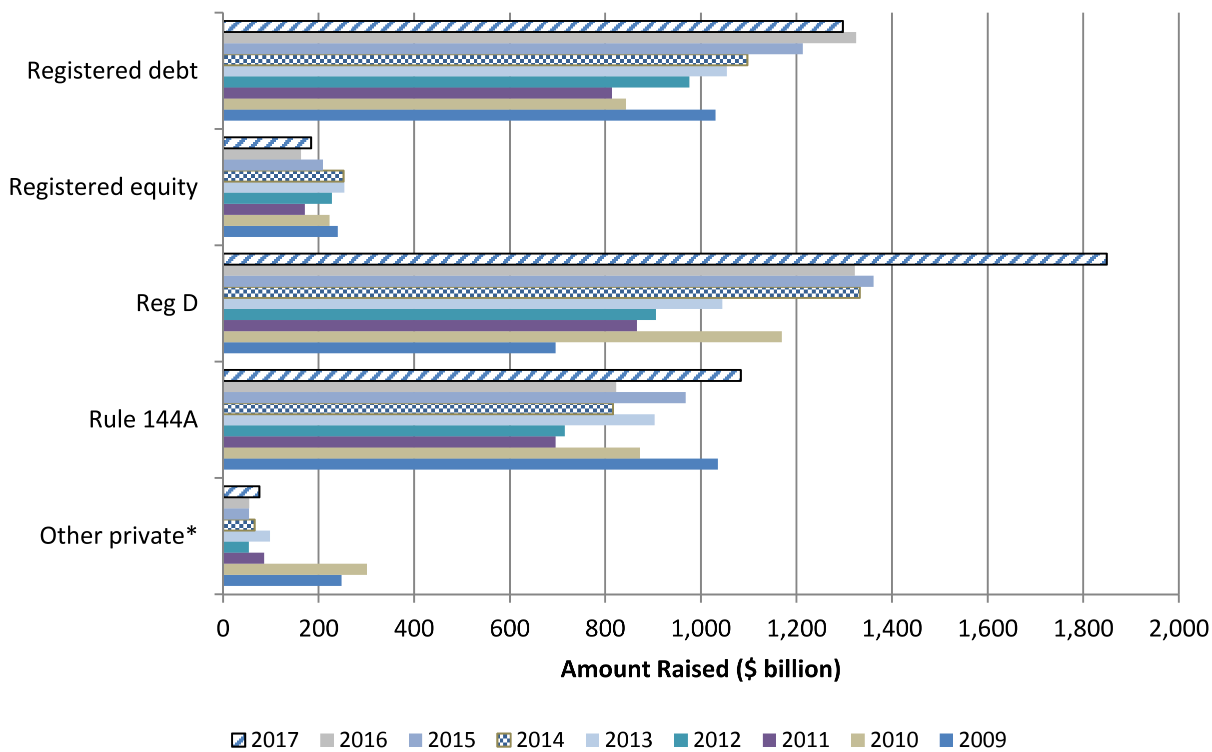
[17] Data on Regulation D offerings was collected from all Form D filings (new filings and amendments) on EDGAR from January 2009 through December 2017; Data on non-ABS Rule 144A offerings was collected from Thomson Financial SDC new Issues database, Dealogic, and the Mergent database. Data on ABS and CMBS Rule 144A offerings was collected from the Asset-Backed Alert and Commercial Mortgage Alert publications; Data for Regulation S offerings was collected from Thomson Financial's SDC Platinum service; Data on Regulation A and Regulation Crowdfunding offerings was collected from all Form 1-A and Form C filings (new filings and amendments) on EDGAR from May 2015 through December 2017; and Data for other private offerings (excluding Regulation A and Regulation Crowdfunding offerings) was collected from Thomson Financial's SDC Platinum, which uses information from underwriters, issuer websites, and issuer SEC filings to compile its Private Issues database. These include offerings under Section 4(a)(2) of the Securities Act that do not claim a Regulation D or Reg S exemption and that are without a follow-on Rule 144A sale. These numbers are accurate only to the extent that SDC is able to collect such information, and may understate the actual amount of capital raised under Section 4(a)(2) if issuers and underwriters do not make this data available.

[18] Separate analysis by DERA staff of Form D filings by funds advised by registered investment advisers and broker-dealer members of FINRA suggests that Form D filings are not made for as much as 10% of unregistered offerings eligible for relief under Regulation D.

Regulation D offerings, $1.8 trillion, is considerably larger than the amount of public debt (straight and convertible debt) and public equity (common and preferred) offerings over the same time.[19] Rule 144A offerings are predominantly debt offerings while Regulation D offerings are mainly equity offerings, although a non-trivial number of the latter include debt securities but the amounts are not separately reported. Within the private capital market, Regulation D and Rule 144A are the dominant offering methods. Over the period 2009-2017, the amount of capital raised through Regulation D offerings is much larger than, the amount of capital raised under Rule 144A.[20]

**Figure 1.** Aggregate capital raised in 2009-2017 by offering method ($billions)




* Other private includes Regulation S offerings, Section 4(a)(2) offerings, Regulation Crowdfunding offerings, and Regulation A offerings.

[19] Data for registered debt and equity offerings from Thomson Financial's SDC Platinum.

[20] By its terms, Rule 144A is available solely for resale transactions. However, market participants use it to facilitate capital-raising by issuers by means of a two-step process, in which the first step is a primary offering on an exempt basis to one or more financial intermediaries, and the second step is a resale to "qualified institutional buyers" in reliance on Rule 144A.

Table 1 estimates the size of the private and public markets in terms of number of offerings per year. As the table shows, offerings in the private market occur with a significantly higher frequency compared to public market issuances. Regulation D offerings occur with far greater frequency than any other offering method surveyed, indicating that the accumulation of capital raised through Regulation D occurs by way of much smaller offering denominations than other methods. This finding is consistent with Regulation D being the primary tool for capital raising by smaller entities. In contrast, Rule 144A offerings are larger in dollar terms, reflecting its use by larger issuers. The large increase in 'Other private offerings' in 2017 compared to previous years comes mainly from Regulation Crowdfunding and Regulation A offerings.

**Table 1.** Number of offerings by type of offering and year

| | **Public Offerings** | | **Private Offerings** | | |
|---|---|---|---|---|---|
| Year | Public equity | Public debt | Regulation D | Rule 144A | Other private* |
| 2009 | 942 | 1,445 | 18,295 | 1,661 | 942 |
| 2010 | 1,072 | 1,930 | 25,993 | 1,958 | 930 |
| 2011 | 863 | 1,465 | 27,336 | 1,388 | 960 |
| 2012 | 954 | 1,473 | 28,184 | 1,558 | 531 |
| 2013 | 1,250 | 1,510 | 30,429 | 1,896 | 841 |
| 2014 | 1,176 | 1,576 | 33,429 | 1,813 | 674 |
| 2015 | 985 | 1,565 | 34,877 | 1,761 | 287 |
| 2016 | 821 | 1,636 | 35,793 | 1,500 | 450 |
| 2017 | 976 | 1,846 | 37,785 | 2,099 | 1,217 |

*Includes offerings conducted under Regulation S, qualified Regulation A, Regulation Crowdfunding, and Section 4(a)(2).

## III. The Regulation D market

Regulation D was promulgated in 1982 to provide a unified scheme for exempting certain capital offerings from registration requirements. It was designed to simplify existing rules and regulations to facilitate capital formation, particularly for small businesses, consistent with the protection of investors. At its inception, the Regulation D market was comprised of three rules: Rule 504, Rule 505, and Rule 506.

Rule 506 was amended pursuant to Title II of the JOBS Act, which directed the Commission to permit general solicitation and general advertising in Rule 506 offerings.[21] Rule 506(c) became effective on September 23, 2013 and allows for general solicitation and

[21] Pub. L. No. 112-106, § 201(a), 126 Stat. 306, 313 (Apr. 5, 2012).

advertising in Rule 506 offerings as long as all purchasers are accredited investors and issuers take reasonable steps to verify that such purchasers are accredited investors.[22] Rule 506, as it existed before the adoption of Rule 506(c), was preserved and re-designated as Rule 506(b).

As noted above, in view of the low levels of usage of Rule 505, SEC recently repealed the Rule 505 exemption, effective May 22, 2017.[23] At the same time, the Commission amended Rule 504 to increase the aggregate amount of securities that may be offered and sold in a 12-month period, from $1 million to $5 million.[24] In addition to being more reflective of contemporary seed-capital needs of early stage companies, the higher ceiling under Rule 504 was adopted to facilitate the development of regional offerings, and intrastate crowdfunding offerings.

The tables and figures in this section provide a broad overview of capital formation in the Regulation D capital market and its various exemptions. The information in this section, as well as the following Section IV, that provides a detailed analysis of the characteristics of Regulation D market participants is based on information reported in Forms D and D/A filed by issuers of such offerings.

### a. Capital raised in Regulation D market

Analysis of issuer self-reported data through electronic Form D filings in Table 2 reveals that the number of unregistered offerings and corresponding amounts raised have been increasing over the years 2009-2017.[25]

**Table 2.** Capital raised through Regulation D and Regulation D/A (amended) offerings*

| Year | Regulation D filings (number) | Regulation D/A filings (number) | Total amount sold ($ Billions) | Mean amount sold ($ millions) | Median amount sold* ($ millions) |
|---|---|---|---|---|---|
| 2009 | 13,764 | 7,077 | 595 | 36 | 1.5 |
| 2010 | 17,581 | 11,864 | 1,025 | 26 | 1.4 |
| 2011 | 18,174 | 12,536 | 863 | 28 | 1.5 |
| 2012 | 18,187 | 13,284 | 903 | 27 | 1.5 |
| 2013 | 19,846 | 14,533 | 1,029 | 24 | 1.5 |
| 2014 | 22,004 | 15,254 | 1,332 | 24 | 1.5 |
| 2015 | 22,853 | 15,649 | 1,361 | 25 | 1.5 |

[22] Eliminating the Prohibition Against General Solicitation and General Advertising in Rule 506 and Rule 144A Offerings, Release No. 33-9415 (July 10, 2013) ("Rule 506(c) Adopting Release"). General solicitation had not been allowed for Rule 506 offerings since its enactment in 1982 as a non-exclusive safe harbor under Section 4(a)(2) of the Securities Act of 1933.

[23] *See* fn. 7 above.

[24] *Id.,* The new provisions of Rule 504 became effective in January 20, 2017.

| | | | | | |
|---|---|---|---|---|---|
| 2016 | 22,991 | 16,490 | 1,322 | 24 | 1.5 |
| 2017 | 24,476 | 17,192 | 1,849 | 32 | 2 |

*Mean and median amount sold based on initial (new) Form D filings only. Total amount sold includes additional amounts raised and reported in amended filings, recorded at the time of the amendment.

These estimates are based on the reported "total amount sold" at the time of the original filing – required within 15 days of the first sale – as well as any additional capital raised and reported in amended filings. The data likely underreport the actual amount sold due to two factors. First, because electronic filings were phased-in through the end of March 2009, paper filings in the first quarter of 2009 are not captured in the analysis. Underreporting could occur in all years because Regulation D filings can be made prior to the completion of the offering, and amendments to reflect additional amounts sold generally are not required if the offering is completed within one year and the amount sold does not exceed the original offering size by more than 10%. Second, as previously described, Rule 503 requires the filing of a notice on Form D, but filing a Form D is not a condition to claiming a Regulation D safe harbor or exemption. Hence, it is possible that some issuers do not file a Form D for offerings relying on Regulation D.[26] Finally, in their annual amendments, some funds appear to report net asset values for total amount sold under the offering. Net asset values could reflect fund performance as well as new investment into, and redemptions from, the fund. Based on Form D data, it is not possible to distinguish between the two impacts.

### b. Cyclicality

It is a well-documented empirical fact that public capital markets are cyclical and the cyclicality appears to be driven by the business cycle, investor sentiment, and time-varying information asymmetry.[27] However, there is little empirical evidence on the cyclicality of capital raised through private offering markets, and in particular, whether issuers rely more on private markets when public markets are under distress (e.g., during recessions).

Figure 2 shows Regulation D offering activity based on the number of offerings by calendar year, relative to the S&P 500 index, for the period 1993-2017. These numbers correspond to all new (non-amended) Form D filings on the EDGAR filing system. While the data does not indicate the aggregate amount raised through these offerings, Table 2 shows that

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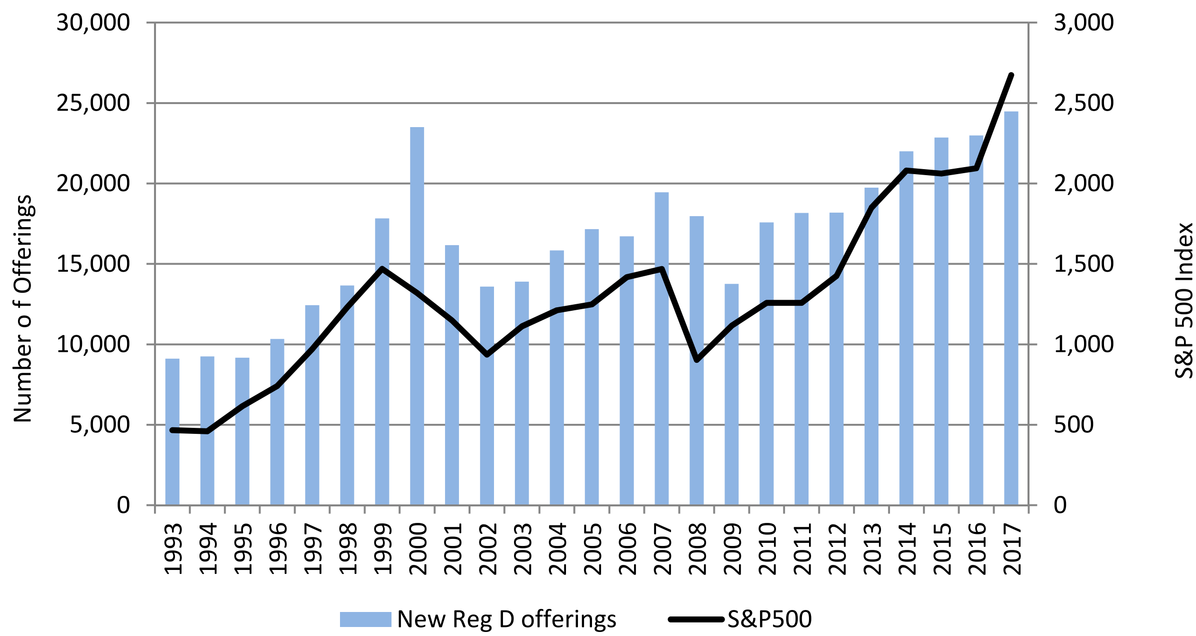
[26] Separate analysis by DERA staff of Form D filings by funds advised by registered investment advisers and broker-dealer members of FINRA during the period 2009-2011 suggests that Form D filings are not made for as much as 10% of unregistered offerings eligible for relief under Regulation D.

[27] *See* Ivanov, I. and C. Lewis, *The Determinants of Market-Wide Issue Cycles for Initial Public Offerings*, Journal of Corporate Finance, December 2008; Lowry, M., *Why Does IPO Volume Fluctuate So Much?*, Journal of Financial Economics, January 2003; and Choe,H. , R. Masulis and V. Nanda: *Common Stock Offerings Across the Business Cycle: Theory and Evidenc*e, Journal of Empirical Finance, June 1993.

offering sizes, on average, are fairly constant over the most recent five years, suggesting that the year-to-year changes in the number of offerings may also track changes in the amounts sold.

**Figure 2.** Number of Regulation D offerings: 1993-2017

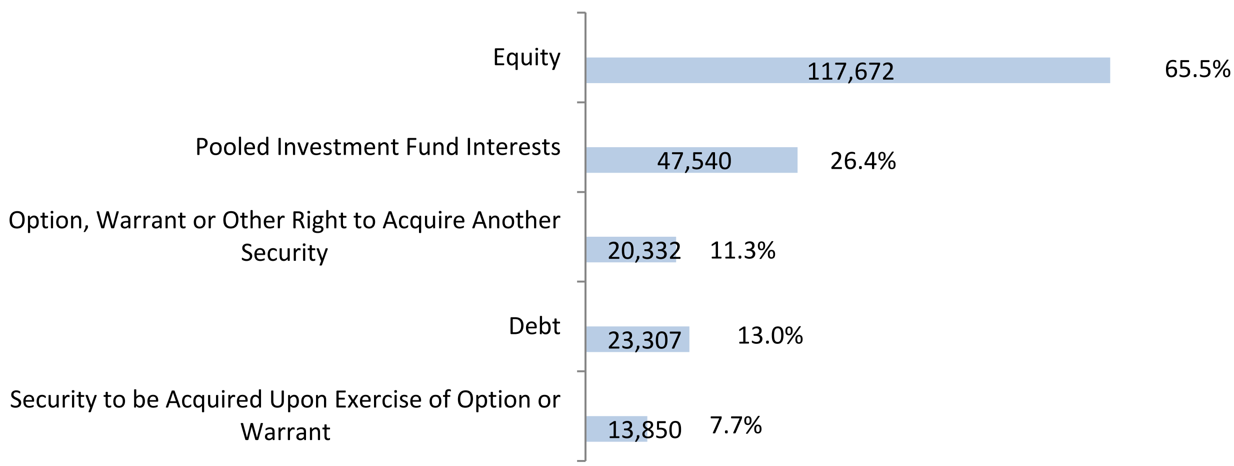



The time series of offering activity shows that subsequent to an increase in new Regulation D offerings during the early 2000s, there was a decline in 2008 that worsened in 2009 consistent with the onset of the financial crisis. More broadly, there is a strong, positive correlation of the incidence of new Regulation D offerings with the economic condition of the public market. In particular, the level of Regulation D offering activity closely follows the level of the S&P 500 index (correlation of 89% during 1993-2017). There were peaks in the number of Regulation D offerings in 2000 and 2007, consistent with heightened stock market valuations. Since the resolution of the recent financial crisis, the past 8 years have seen a considerable increase in Regulation D offering activity, in line with the increases in the S&P 500 index (correlation of 94% during 2009-2017). Hence, private offerings in the Regulation D market appear to be pro-cyclical, suggesting that the health of the private capital market is closely tied to that of the public capital market.

### c. Offering Security Type

The importance of the Regulation D market is magnified when considering that approximately two-thirds of Regulation D offerings represent new equity capital (Figure 3), unlike public capital markets where the majority of capital raised in new offerings is related to fixed maturity debt. Equity is a more permanent source of capital than debt, and thus its issuance is more likely to reflect new investment as opposed to debt, which is often used to refinance existing debt. Put differently, to the extent that debt offerings are attributed to the "rolling over" of existing debt due to an expiring term or refinancing due to a change in interest rate environment, such transactions do not reflect the financing of new investment.[28] In addition, a larger fraction of non-financial issuers rely on Regulation D for raising capital compared to the Rule 144A market, where the vast majority of issuers are financial institutions and over 99% of securities are debt securities.

**Figure 3**. Number and percent of Regulation D offerings by type of security issued: 2009-2017[29]



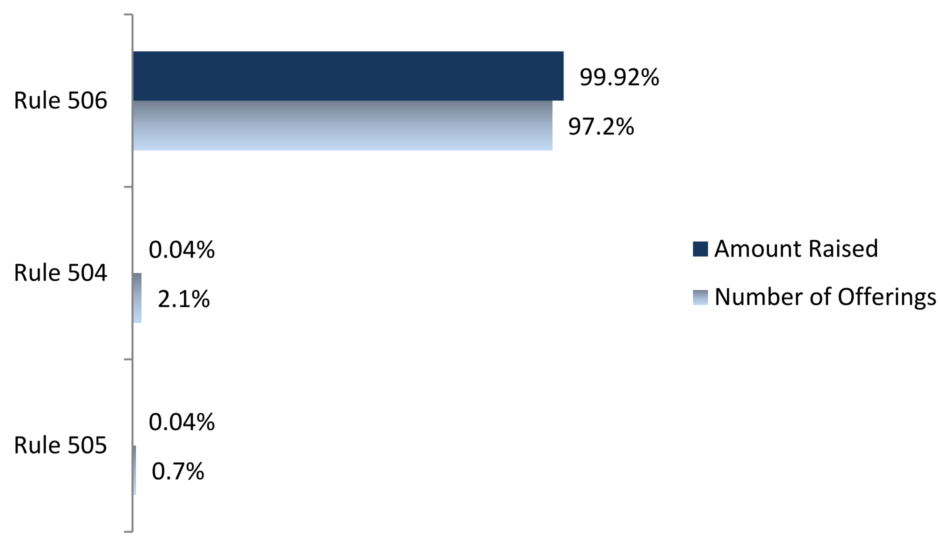

### d. Prevalence of Rule 506

Consistent with previous findings,[30] Rule 506 continues to be the predominant capital market for private offerings under Regulation D. Securities issued under Rule 506 are considered "covered securities" pursuant to Section 18 of the Securities Act, and are thus exempt from state securities law registration and qualification requirements. Most Regulation D offerings (97% since 2009, see Figure 4) are issued under Rule 506. Rule 506 offerings accounted for approximately 99.9% of the reported capital raised through Regulation D

[28] It is possible that equity issuances in Regulation D offerings reflect deleveraging – conversion of debt to equity, which may not reflect new investment.
[29] There are 222,701 issues referenced, which is greater than the total 179,771new issues in Table 2. This is due to multiple securities listed in the same filing.
[30] See the 2015 Unregistered Offerings Study

offerings since 2009. Even among Regulation D offerings under $5 million in size, for which Rule 504 offerings are currently (and Rule 505 offerings were historically) possible, Rule 506 accounts for almost 98% of the capital raised.[31] Similarly, for offerings under $1 million by non-fund issuers, for which Rule 504 offerings were historically one possibility, Rule 506 accounted for approximately 93% of the capital raised. Unlike 506 offerings, Rule 504 are (and Rule 505 offerings were) subject to state registration laws, suggesting that the more restrictive provisions of Rule 506 are less important than state securities law preemption (e.g., Rule 506(b) limits the participation of non-accredited investors to 35 per offering, prohibits general solicitation, and the securities issued in Rule 506 offerings are restricted securities, whereas Rule 504 allows for an unlimited number of non-accredited investors and may, under certain circumstances, permit general solicitation and result in the issuance of unrestricted securities).[32]

**Figure 4.** Fraction of offerings and amount raised by Regulation D Exemption: 2009-2017




It remains to be seen if the increase in Rule 504 maximum offer amounts and the availability of regional and crowdfunding offerings will increase the usage of the Rule 504 exemption. At least in the first year, it appears that there has been an uptick in the number of new offerings that claimed Rule 504 exemption. New Rule 504 offerings during 2017 increased by approximately 21%, relative to new Rule 504 offerings in 2016 (underlying data in table 6 below; Rule 504 offerings had declined by 16% and 4% in the previous 2 years).

[31] *See* Section IIId(ii) for Regulation D offerings by exemption and offering size.
[32] *See* discussion of Rules 504, 505, and 506 or Regulation D at http://www.sec.gov/answers/regd.htm

### i. The new Rule 506(c) market

From September 23, 2013 to December 31, 2017, a total of 6,690 issuers initiated 7,110 new Rule 506(c) offerings (Table 3). During this period, based on initial Form D filings, almost $183.3 billion was reported raised. An additional $72 billion was reported raised in amendments to initial filings, some of which were originally initiated as Rule 506(b) offerings. During the same period, there were 87,890 new Rule 506(b) offerings that reported to raise $1.8 trillion in their initial Form D filings, and an incremental amount of $4.0 trillion was reported to be raised in amendments filed. On a relative basis, issuances claiming the new Rule 506(c) exemption have accounted for only 4.4% of the reported capital raised pursuant to Rule 506 since becoming effective in September 2013.

While the underlying motivation for permitting general solicitation was to boost capital formation through increased accessibility of certain issuers to accredited investors, the vast majority of Regulation D issuers continue to raise capital through rule 506(b) offerings. The relative novelty of the 506(c) provisions after decades of non-permissibility of general solicitation in Regulation D offerings may be one reason why Rule 506(b) continues to dominate the Regulation D market. In particular, issuers with pre-existing sources of financing and/or intermediation channels may not yet have a need for the new flexibility. Other issuers may become more comfortable with market practices as they develop over time, including among other things, certainty over what constitutes general solicitation.[33] Some issuers may be reluctant to use general solicitation to avoid sharing information publicly (through Form D filings or through advertising materials), for competitive and general business reasons.[34] There may also be concerns about the added burden or appropriate levels of verification of the accredited investor status of all purchasers,[35] for which efficient market solutions may develop over time. Regulatory uncertainty has also been previously identified as a possible explanation for the relatively low level of the Rule 506(c) offerings.[36]

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[33] *See*, for example Keith Higgins, Director of the Division of Corporation Finance, U.S. Securities and Exchange Commission, Remarks before the 2014 Angel Capital Association Conference (Mar 28, 2014) available at: (http://www.sec.gov/News/Speech/Detail/Speech/1370541320533. *See* also comments of Jean Peters, Board member, Angel Capital Association, at the 33rd Securities & Exchange Commission Government-Business Forum on Small Business Capital Formation, November 20, 2014.

[34] *See*, https://www.bna.com/rule-506cs-general-b73014451604/. *See* also, comments of Jean Peters, Board member, Angel Capital Association, at the 33rd Securities & Exchange Commission Government-Business Forum on Small Business Capital Formation, November 20, 2014.

[35] *Id.*

[36] *See*, for example, https://dealflow.com/whitepapers/Dealflow_White_Paper_Q3_2014.pdf

**Table 3:** Capital Raising Activity in Rule 506(b) and Rule 506(c) Markets during 2013-2017

| | Number of New Offerings | | | Amounts Raised ($ million) | | |
|---|---|---|---|---|---|---|
| | Rule 506(b) | Rule 506(c) | Proportion Rule 506(c) | Rule 506(b) | Rule 506(c) | Proportion Rule 506(c) |
| 2013 * | 4,940 | 506 | 9.3% | $214,826 | $8,748 | 3.9% |
| 2014 | 19,560 | 1,611 | 7.6% | $1,323,146 | $23,837 | 1.8% |
| 2015 | 20,563 | 1,592 | 7.2% | $1,321,417 | $39,370 | 2.9% |
| 2016 | 20,707 | 1,665 | 7.4% | $1,285,853 | $35,952 | 2.7% |
| 2017 | 22,120 | 1,736 | 7.3% | $1,700,045 | $147,310 | 8.0% |
| 2013-2017 | 87,890 | 7,110 | 8.1% | $5,845,288 | $255,216 | 4.4% |

** September 23, 2013 - December 31, 2013*

Additional analysis in Table 4 shows that although the average amount reported sold in an initial Rule 506(c) offering ($41 million)[37] is much larger than the average amount reported sold in a Rule 506(b) offering ($26 million), the median amount sold in an initial Rule 506(c) offering ($0.8 million) is half the median amount sold in an initial Rule 506(b) offering. The lower amounts reported to be raised at the date of initial filing may be the result of issuers with anticipated difficulties raising capital in a timely manner choosing the Rule 506(c) market so that they have an ability to advertise or generally solicit their offering to a broader audience of potential investors. It is possible that some sophisticated investors may perceive the election of the 506(c) exemption as a signal that issuers anticipate difficulties in raising sufficient capital and consequently consider it a less attractive offering, which could also dissuade issuers from utilizing the new exemption for their financing needs. Another reason for the lower initial amounts reported in the 506(c) market may be that the issuer is selling as it is conducting the general solicitation. After 15 days of the first sale, it has to file the Form D, but continues to sell afterwards. On the other hand, the 506(b) issuer can't do general solicitation, so it already knows who the investors who will purchase will be and by the time of the 15 day deadlines, it has already sold a larger percentage of the offering.

**Table 4.** Capital raised through Rule 506(c) and Rule 506(b) offerings: September 23, 2013 - December 31, 2017

[37] This is due in part to an outlier – a very large 506(c) offering for 93 billion. Excluding the outlier, we find that the average Rule 506(c) offering is also considerably smaller than the average Rule 506(b) offering.

| Exemption | Form D Filings | Number of Amendment Filings | Total amount sold ($ billions) | Mean amount sold ($ millions) | Median amount sold ($ millions) | Median offer size ($ millions) |
|---|---|---|---|---|---|---|
| 506(c) | 7,110 | 2,909 | $255 | $41 | $0.8 | $3.0 |
| 506(b) | 87,890 | 64,253 | $5,845 | $26 | $1.6 | $2.4 |
| All 506 | 95,000 | 67,162 | $6,101 | $27 | $1.5 | $2.5 |
| Regulation D** | 98,030 | 67,681 | $6,103 | $26 | $1.5 | $2.2 |

** Total amount sold includes incremental amounts reported to be raised in amended filings (Form D/As). Mean and median amounts sold based on initial (new) Form D filings only. Median offer size is based on offerings that report their amount of offering.*
*** Includes all four exemptive rules: Rules 504, 505, 506(b) and 506(c).*

A deeper look at amounts raised in the Rule 506(b) and Rule 506(c) markets shows divergent trends for amounts reported to be raised by issuers that are pooled investment funds, relative to non-fund issuers (operating firms and financial firms). Total capital reported to be raised (Forms D and D/A) and initial amounts reported to be raised (Form D) by fund issuers relying on Rule 506(c) exemption increased by 378% and 969% respectively during 2017, relative to the previous year. The comparative data for capital raised by Rule 506(b) fund issuers and non-fund issuers is presented in Table 5.

**Table 5:** Initial Amounts Reported to be Raised in Form D Filings, 2013-2017

| | Amount raised ($M), Funds | | Amount raised ($M), Non-Funds | |
|---|---|---|---|---|
| Period | Rule 506(b) | Rule 506(c) | Rule 506(b) | Rule 506(c) |
| 2013 * | $76,188 | $2,685 | $24,374 | $2,435 |
| 2014 | $281,270 | $4,725 | $127,269 | $7,874 |
| 2015 | $294,769 | $4,217 | $140,258 | $13,872 |
| 2016 | $290,166 | $9,833 | $124,478 | $6,046 |
| 2017 | $355,341 | $105,093 | $129,237 | $26,439 |
| 2016-2017 growth | | | | |
| Forms D only: | 22% | 969% | 4% | 337% |
| Forms D and D/A: | 33% | 378% | 4% | 148% |

** September 23, 2013 - December 31, 2013*

Data trends in Table 5 point to a nascent uptick in capital raised by fund issuers by relying on the Rule 506(c) exemption. Industry reports also indicate that some pooled investment funds have started to re-evaluate the benefits of relying on general solicitation. It remains to be seen if this increased reliance on the Rule 506(c) exemption by fund issuers will develop into a longer-term trend that will expand the Rule 506(c) market, relative to the traditional Rule 506(b) market.

For now, consistent with the somewhat limited uptake of new Rule 506(c), there has not been significant migration of existing issuer capital raising activity from Rule 506(b) to Rule 506(c). There has been some movement in the number of "repeat" issuers that have switched their offering types from a non-Rule 506(c) to Rule 506(c): Almost 1,574 new Rule 506(c) offerings (22% of all new Rule 506(c) offerings) were initiated by 1,101 issuers that also conducted another Regulation D offering that relied on an exemption other than Rule 506(c).

Capital raising activity in Rule 506(c) market does not appear to be associated with a decline in the overall capital formation in the Rule 506(b) market relative to previous years. In fact, Table 6 below shows that there was an increase in the number of Rule 506(b) offerings in 2017 to over 22,100 new Rule 506(b) offerings compared to approximately 18,400 new Rule 506(b) offerings in 2013 (when Rule 506(c) became effective) and 17,300 in 2012. In contrast, there was a period of decline in new Rule 504 offerings, which, under certain circumstances, permits issuers to advertise their offerings, while requiring registration at the state level. However, the decline in Rule 504 offerings continued from prior years, and therefore may not be entirely due to the emergence of the Rule 506(c) capital market. Additionally, the Rule 504 offerings market rebounded in 2017, reaching a number of offerings closer to that in 2014.

**Table 6.** Number of new offerings in Regulation D markets

| Exemption | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 |
|---|---|---|---|---|---|---|---|---|---|
| Rule 504 | 579 | 714 | 721 | 632 | 599 | 544 | 524 | 443 | 536 |
| Rule 505* | 195 | 262 | 207 | 227 | 229 | 289 | 174 | 176 | 84 |
| Rule 506(b) | 12,935 | 16,559 | 17,199 | 17,262 | 18,407 | 19,560 | 20,563 | 20,707 | 22,120 |
| Rule 506(c) | | | | | 506 | 1,611 | 1,592 | 1,665 | 1,736 |

** Rule 505 was repealed, effective May 22, 2017.*

### ii. Regulation D Offerings by Offering Method and Size

Rule 506 is the dominant offering method even among those offering sizes that were eligible for Rules 504 and were eligible for Rule 505 before its repeal (Tables 7a and 7b). Almost 31% of all Rule 506 offerings (Table 7a) and 36% of Rule 506 offerings by non-funds (Table 7b) since 2009 were for less than $1 million and therefore may have qualified for the Rule 504 exemption based on offering size, but issuers elected to claim the Rule 506 exemption. An additional 30% of all Rule 506 offerings and 35% of Rule 506 offerings by non-fund issuers were for amounts between $1 million and $5 million, and therefore could have claimed a Rule 505 exemption based on offering size. The same picture is evident when considering amount of capital raised (Figure 5). This evidence suggests that the preemption of state securities law registration and qualification requirements in Rule 506 offerings has greater value to issuers than the unique features of Rule 504 or Rule 505 offerings.

With the adoption of Rule 506(c), there is even greater incentive for issuers to use Rule 506. As the third section of Table 7a shows, Rule 506(c), though dwarfed by Rule 506(b), was used more often than Rule 505. While there were a greater number of Rule 504 offerings than Rule 506(c) offerings under $1 million, the downward trajectory in number of new Rule 504 offerings suggests that, under the current scheme of Regulation D rules, Rule 506 will dominate Rule 504 in the near future.

**Table 7a**. Number of new Regulation D offerings, by size and offering method*

| | Offering size | | | |
|---|---|---|---|---|
| | ≤ $1 million | $1-5 million | $5-50 million | >$50 million |
| **<u>All Issuers, 2009-2017</u>** | | | | |
| Rule 504 | 5,112 | 72 | -- | -- |
| Rule 505 | 678 | 1,113 | -- | -- |
| Rule 506 | 50,207 | 49,003 | 45,043 | 20,579 |
| **<u>Non-Fund Issuers, 2009-2017</u>** | | | | |
| Rule 504 | 5,112 | 72 | -- | -- |
| Rule 505 | 650 | 1,029 | -- | -- |
| Rule 506 | 44,036 | 42,965 | 31,539 | 4,689 |
| **<u>Non-Fund Issuers, September 23, 2013 – December 2017</u>** | | | | - |
| Rule 504 | 2,060 | 72 | -- | -- |
| Rule 505 | 308 | 428 | -- | -- |
| Rule 506(b) | 21,683 | 21,587 | 15,623 | 2,256 |
| Rule 506(c) | 1,790 | 1,808 | 1,501 | 289 |

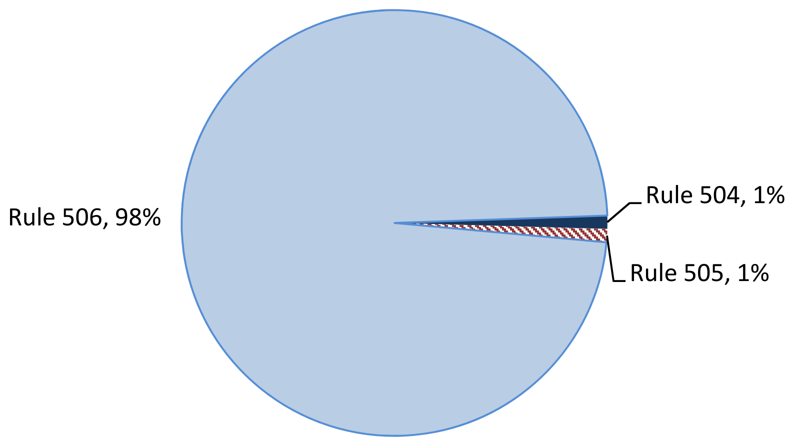
**Considers only new offerings and excludes offerings with amount sold reported as $0 or missing on Form D.*

Since the amendments to Rule 504 became effective in January 2017, there have been 72 new offerings that claimed Rule 504 exemption and offered/raised more than $1 million during the year. The number of new Rule 504 offerings increased by 21% in 2017, relative to a 2.6% increase in new Rule 506 offerings under $5 million initiated by non-fund issuers. It will be interesting to see if the amended Rule 504 market will attract a greater number of smaller offerings, compared to previous years and also how the amended Rule 504 market compares with that of Rule 506 which has so far attracted a substantial proportion of all small offerings.

**Table 7b.** Number of new Rule 504 offerings by non-fund issuers relative to Rule 506 offerings

| | 2015 | | 2016 | | 2017 | |
|---|---|---|---|---|---|---|
| | <=$1 million | $1-$5 million | <=$1 million | $1-$5 million | <=$1 million | $1-$5 million |
| Rule 504 | 524 | 0 | 443 | 0 | 464 | 72 |
| Rule 506 | 5,742 | 5,479 | 5,791 | 5,458 | 5,799 | 5,738 |

**Figure 5**. Fraction of capital raised by exemption in new offerings of up to $5 million: 2009-2017

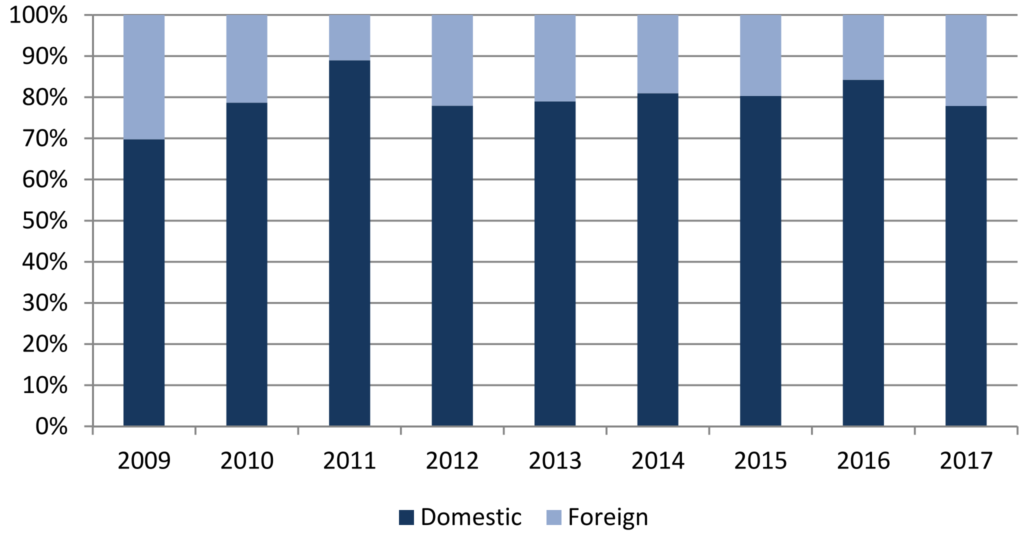



### e. Foreign firms and Exchange Act reporting firms in Regulation D market

The intent of Regulation D and the JOBS Act has been to promote capital formation for small and emerging firms in the U.S., which by and large tend to be private firms.[38] However, foreign firms or public firms in the U.S. are not excluded from using Regulation D. Over the period from 2009 to 2017, foreign issuers account for approximately 20% of all capital raised by Regulation D offerings, although this fraction varies over time (Figure 6). Participation was lowest in 2011 and highest in 2009 (at the height of the financial crisis).

[38] *See* Revision of Certain Exemptions from Registration for Transactions Involving Limited Offers and Sales, Release No. 33-6389 (Mar. 8, 1982) [47 FR 11251]. Also see, *See* Rule 506(c) Adopting Release.

**Figure 6**. Percent of capital raised in U.S. by domestic and foreign issuers in Regulation D offerings




Issuers incorporated in Cayman Islands, Canada and United Kingdom accounted for more than 80% of foreign participation in terms of number of new offerings.

Issuers that file periodic reports with the Commission under the Securities Exchange Act of 1934 often conduct private offerings. [39] It is interesting to note that some of these firms choose to raise capital in a private market, even though they have access to the more liquid and larger public market. Reasons why public firms could be issuing securities privately could include asymmetric information between managers and investors and market timing. A number of academic studies[40] have shown that private investors are likely to have better information for reasons like being directly involved in the due diligence process or having signed non-disclosure agreements, which would mitigate, to some extent, the issue of asymmetric information, and thereby improve the informational efficiency of the private capital market. At the same time, issuers can avoid the higher costs associated with public disclosure, thereby lowering the cost of raising capital through unregistered offerings. Additionally, a large proportion of investors in Rule 506 offerings are accredited investors who are considered to be more sophisticated investors that are willing and able to take more risk. Over the nine-year

[39] We identified reporting companies as those that filed on Forms 10-K, 20-F, or 40-F during the analysis period.
[40] *See* for example, Armando Gomes and Gordon Phillips, "*Why do public firms issue private and public securities*", Journal of Financial Intermediation, 21 (2012); Hsuan-Chi Chen, Na Dai and John D. Schatzberg, "*The choice of equity selling mechanisms: PIPES vs SEOs*", The Journal of Corporate Finance, 16 (2010); or Susan Chaplinsky and David Haushalter, "*Financing under extreme risk: contract terms and returns to private investments in public equity*", The Review of Financial Studies, (2010).

analysis period, 8% of Regulation D non-fund offerings were conducted by Exchange Act reporting companies. In addition, about 4% of non-fund offerings were by issuers that subsequently registered an offering with the Commission by filing a Form S-1. For these issuers, a Regulation D offering was a precursor to going public.

## IV. Regulation D market participants

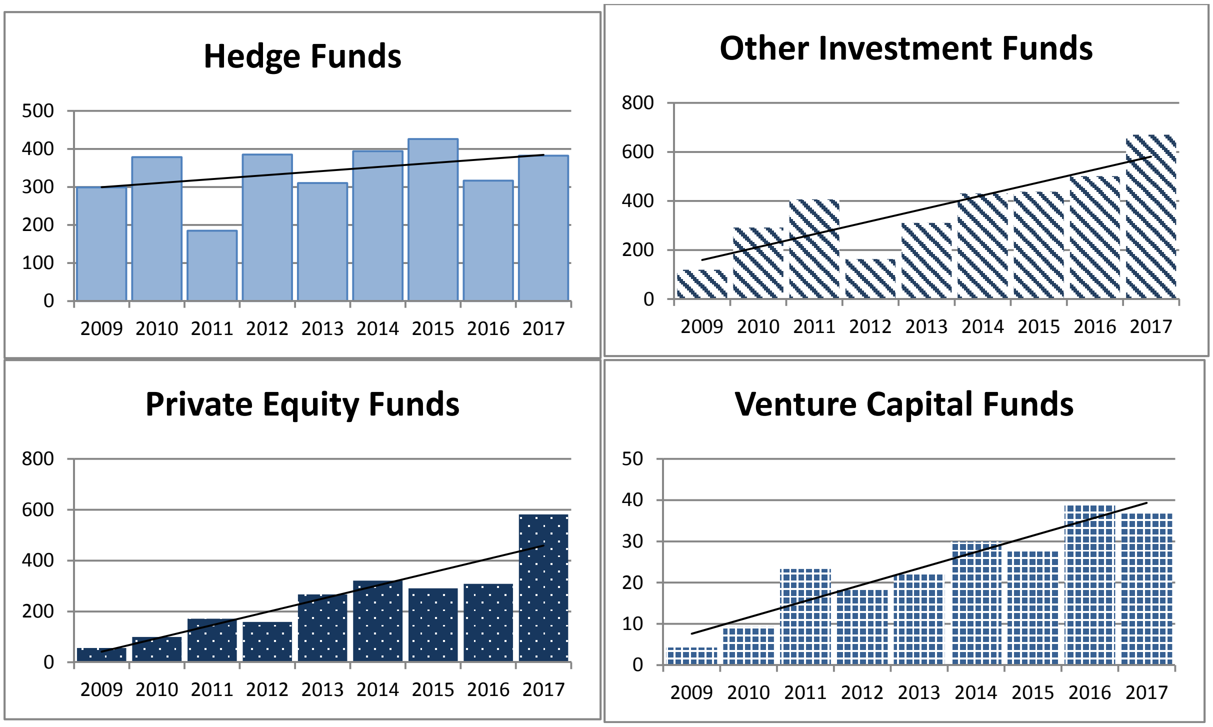
### a. Issuers of securities under Regulation D

#### i. Capital formation and offering activity by issuer type

The largest issuers in the Regulation D capital market, by amount sold, are pooled investment funds that are classified in Form D filings as hedge funds, venture capital funds, private equity funds, and other pooled investment funds. The predominant entities among other pooled investment funds are registered investment companies and commodity pools.[41] Since the inception of the electronic Form D filings in 2009, pooled investment funds have accounted for $8.9 trillion of new capital raised through Regulation D offerings and reported on Form D, compared to $1.42 trillion raised by non-funds. Hedge funds are the largest private fund issuer, and raised almost $3.1 trillion of new capital, of which $382 billion was raised in 2017. In terms of amounts raised by fund, private equity funds raised the largest median amount. A break-up of capital raised by type of private fund over the past eight years shows an increasing trend for all types of funds (Figure 7).

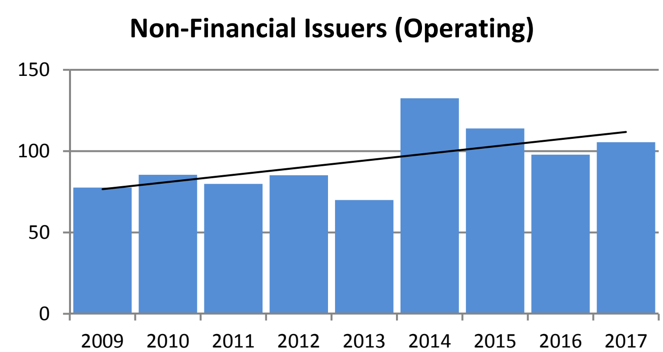
**Figure 7.** Aggregate capital raised (amount sold) during the period 2009-2017 by fund-issuer type ($billion)

[41] Registered investment companies are entities such as mutual funds that issue securities to investors, hold pools of securities and other assets and are registered with the Commission under the Investment Company Act. Commodity pools are investment trusts, syndicates, or similar enterprises that are operated for the purpose of trading commodity futures.



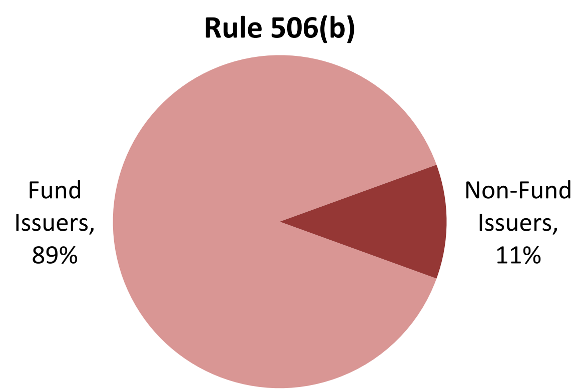

Financial services, including banking, real estate and insurance, accounted for $570 billion raised during the eight-year period. Non-financial issuers, typically private operating companies, raised $848 billion during the eight-year period, of which $105 billion was raised in 2017. Analyzing on a year-to-year basis, Figure 8 shows that capital raised by operating firms has shown an increasing trend, with more than $300 billion raised in the past 3 years.

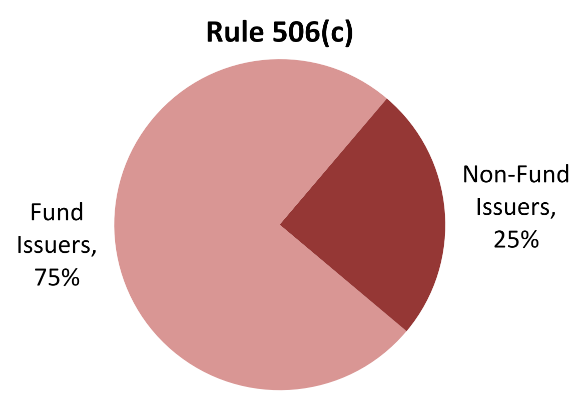
**Figure 8.** Aggregate capital raised (amount sold) during the period 2009-2017 by operating firms ($billions)




As shown in Figure 9, the share of capital raised by non-fund issuers (operating firms, financial firms and real estate firms) is smaller than the share of fund issuers in Rule 506(c) as well as the Rule 506(b) market. However, relative to the Rule 506(b) market, capital raised in Rule 506(c) offerings by non-fund issuers formed a larger proportion. During the last quarter of 2013 and the years 2014-2017, non-fund offerings raised 31% of capital reported to be raised in initial filings for Rule 506(c) offerings. In comparison, only 30% of capital raised in Rule 506(b) market was reported to be raised by non-fund issuers over the same period of time. The share of non-fund issuers declines when incremental amounts reported in amendments are included. The proportion of capital raised by non-fund issuers decreases from 31% to 25% in the Rule 506(c) market, compared with 11% in the Rule 506(b) market.

**Figure 9.** Amounts raised by fund and non-fund issuers in Rule 506 market: September 23, 2013 - December 31, 2017




Although non-fund issuers raised substantially less than fund issuers in the aggregate Regulation D market, they account for the majority of all new offerings and Form D filings (Figure 10 and Figure 11). While hedge funds appear to initiate fewer new offerings, all other types of private funds as well as operating issuers have initiated new offerings on an increasing basis over the period 2009-2017 (Figure 11).

**Figure 10.** Number of initial (new) offerings during the period 2009-2017 by non-fund issuers

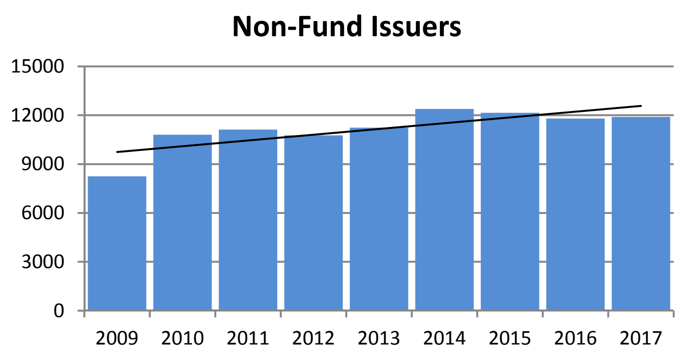
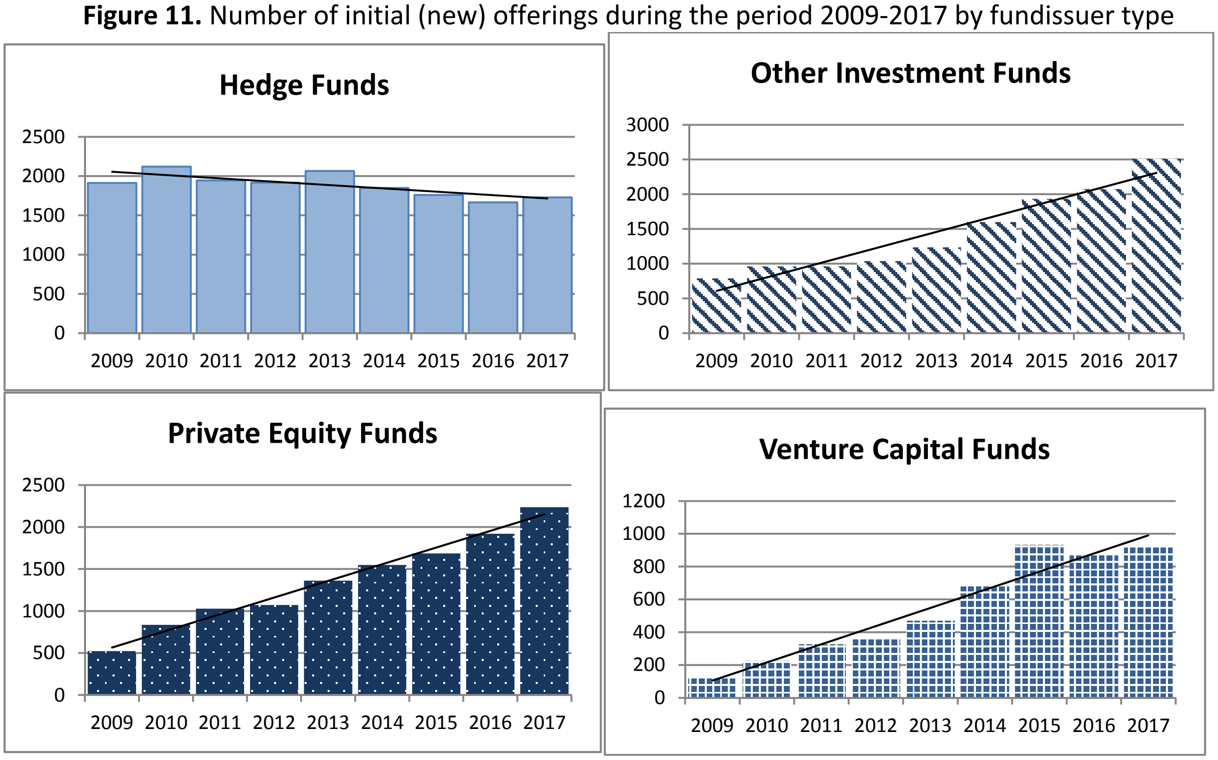
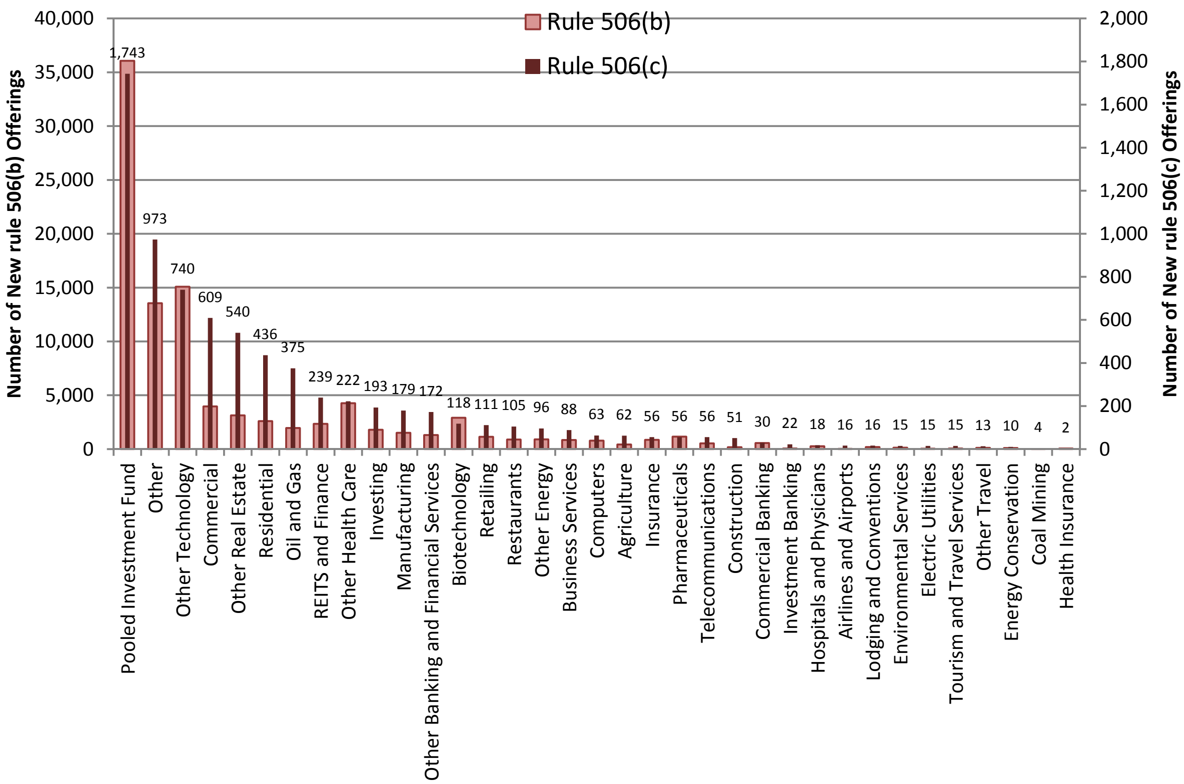



**Figure 11.** Number of initial (new) offerings during the period 2009-2017 by fundissuer type




Offerings by non-fund issuers have so far, also constituted a larger proportion of the Rule 506(c) market, relative to Rule 506(b) market. Non-fund issuers initiated almost three-fourth of new offerings in both Rule 506(b) and Rule 506(c) market. Analyzing all offerings, i.e. new and those continuing from previous years, non-fund issuances are almost 77% of all Rule 506(c) offerings but only 64% of all Rule 506(b) offerings. Most of the non-fund Rule 506(c)offerings are from 'Other', 'Other Technology', 'Commercial', 'Other Real Estate', and 'Residential industries (Figure 12).

**Figure 12.** Number of New Offerings by Industry: September 23, 2013 - December 31, 2017




Similar to Rule 506(b) offerings of fund issuers, among Rule 506(c) issuers that are pooled investment funds, other investment funds are the most dominant issuers in terms of number of new offerings (Table 8). Data in Table 5 (Section III(d)(i) above) shows that capital raised by Rule 506(c) fund issuers increased substantially during 2017, relative to the previous year and also compared to capital raised by Rule 506(c) non-fund issuers and Rule 506(b) fund issuers. Market analysts have also noted the recent uptick in private funds, especially hedge funds, relying on Rule 506(c) exemption, mainly to target larger and institutional investors.[42]

[42] *See*, for example, http://fundfire.com/c/1686623/197263 which states that hedge funds may be relying on Rule 506(c) as a risk mitigation strategy to ensure compliance with SEC rules.

**Table 8.** Amount sold by Rule 506(c) fund issuers: September 23, 2013 - December 31, 2017[43]

| | Number of New Offerings | | Amount sold ($ billions)* | | Median amount sold* ($ millions) | |
|---|---|---|---|---|---|---|
| | 506(c) | 506(b) | 506(c) | 506(b) | 506(c) | 506(b) |
| Hedge Fund | 334 | 7,134 | 29.1 | 1,546.3 | 5.9 | 12.6 |
| Private Equity Fund | 277 | 7,541 | 103.8 | 1,489.2 | 2.0 | 25.0 |
| Venture Capital Fund | 344 | 3,193 | 1.6 | 135.5 | 0.4 | 2.6 |
| Other Investment Fund | 583 | 7,857 | 57.3 | 2,024.9 | 2.0 | 2.8 |
| Non-Funds | 1,538 | 25,725 | 191.6 | 5,195.9 | 1.3 | 9.0 |

** Amount sold includes amount reported in Form D and Form D/A filings. Median amounts are calculated based on non-zero amounts reported in Form D.*

### ii. Average and Median Offering Size by Issuer Type

Consistent with the large number of non-financial offerings and the smaller proportion of capital raised in the Regulation D market, the median offering size for non-financial issuers is substantially lower than the median offering size for funds. During the period 2009-2017, the median offer size of non-financial issuers was $1 million compared to $25 million for hedge funds, and $35 million for private equity funds (Table 9). The differences in mean offering size are even larger. This indicates a large number of small offerings by non-financial issuers, consistent with the original regulatory objective to target the capital formation needs of small businesses.[44] The summary statistics in Table 2 also indicates that a large fraction of offerings are amendments to previously filed offerings, mostly attributed to the continuation of private fund offerings discussed in more detail below. Underscoring the importance of the Regulation D market as a source of capital to smaller firms, a significant number of issuers have relied on this market over the period under consideration. There were 134,345 unique issuers of new Regulation D offerings over the nine years under consideration.[45]

[43] More than 41% of Rule 506(c) fund offerings report their offering amount to be 'Indefinite' (compared to 63% of fund issuances in the Rule 506(b) market).
[44] See note 37.
[45] We identify unique issuers by SEC issued 'CIK' number. It is to be noted that though a number of fund issuers have different CIKs, a number of such fund issuers could belong to the same fund family. As a result, the number of unique issuers could be an overestimate.

**Table 9.** Mean and median offer size for Regulation D offerings in 2009-2017 by issuer type*

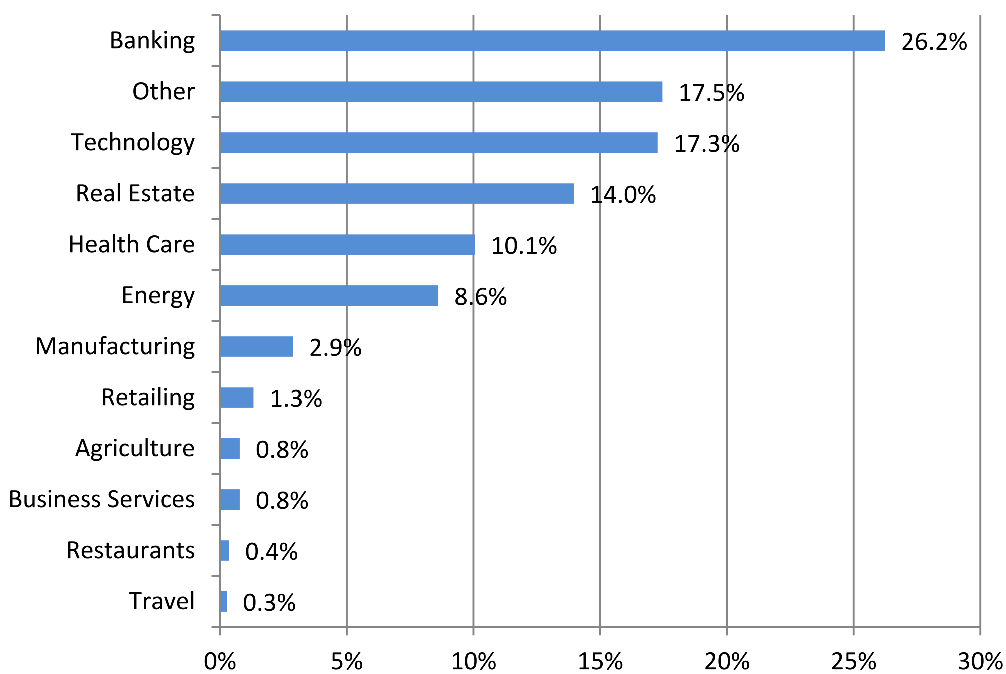
| | Mean offer size ($Millions) | Median offer size ($Millions) |
|---|---|---|
| Hedge Funds | 147 | 25 |
| Private Equity Funds | 241 | 35 |
| Venture Capital Funds | 58 | 4 |
| Other Investment Funds | 226 | 8 |
| Financial Services | 43 | 2 |
| Real Estate | 11 | 2 |
| Non-financial Issuers (operating) | 9 | 1 |

* *Mean and median offer size are based on amount sold reported in initial (new) Form D filings only.*

### iii. Non-Fund Issuers

Overall, for all the exemptions under Regulation D, the largest non-fund industry group by dollar amount sold is Banking, followed by Technology, Real Estate, Health Care, and Energy (Figure 13). The share of Technology sector has increased in recent years due to a few large offerings, while the share of Banking, and Manufacturing industries in the total amounts sold in this market has relatively declined.

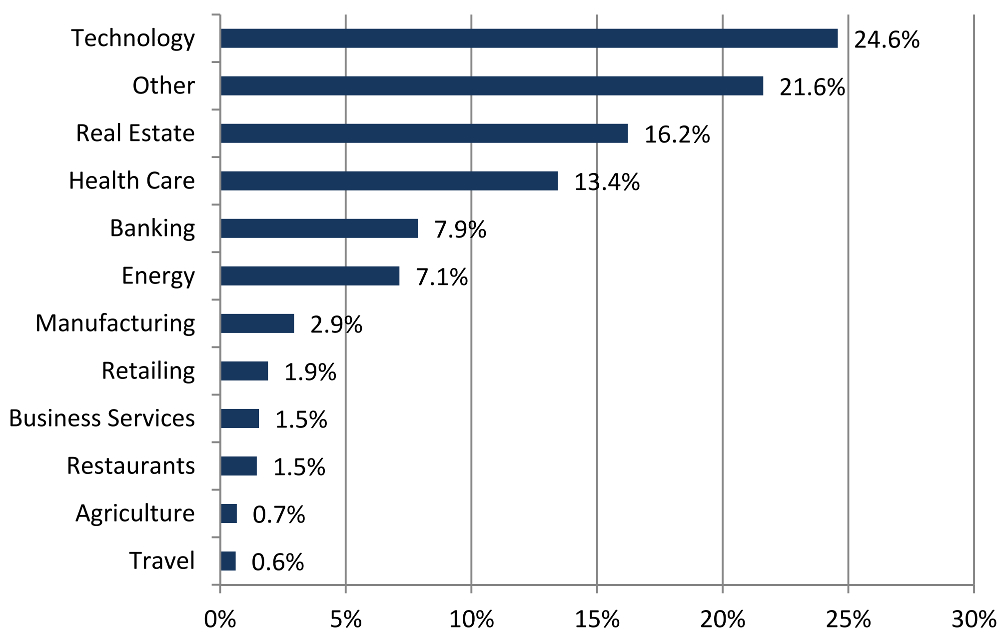
**Figure 13**. Most active non-fund issuers by amount sold: 2009 -2017



Similar to the overall Regulation D market, the most active industries in the Rule 506(c) market, in terms of amounts sold, are the Financial companies and Technology industry (includes Computers, Other Technology and Biotechnology) followed by the Commercial and Other sectors. Approximately 93% of non-fund issuances in Rule 506(c) market reported their offering amount. The remaining did not report their offering amount, or stated it to be 'Indefinite'. Of the ones that report offer size, 23% had raised the entire offering amount and more than 6% of all non-fund offerings had raised at-least three-quarters of their offering amount by date of initial filing. Compared to Rule 506(c) market, 45% of non-fund offerings in Rule 506(b) market had raised the entire offering amount, and almost 11% of the offerings reported raising at-least three-fourths of the total offering amount by the date of initial filing. As discussed earlier, these numbers could indicate either that issuers anticipating difficulty in attracting related persons to subscribe to their offering are more likely to self-select to raise capital pursuant to Rule 506(c), or that Rule 506(c) issuers continue selling securities as they are conducting the general solicitation. As issuers are not required to file a Form D upon completion or termination of their offering, it is not known if their choice of an advertised unregistered offering enables them to successfully raise the desired amount of capital.

Issuers from the Technology industry group are the most active amongst non-fund issuers by number of offerings, comprising about 25% of all reported non-fund offerings (Figure 14) in the Regulation D market. This is not surprising, given the predominance of private investment in start-ups and small firms in this sector. Approximately one-fifth of offerings (22%) do not specify an industry on Form D, and check 'Other'.

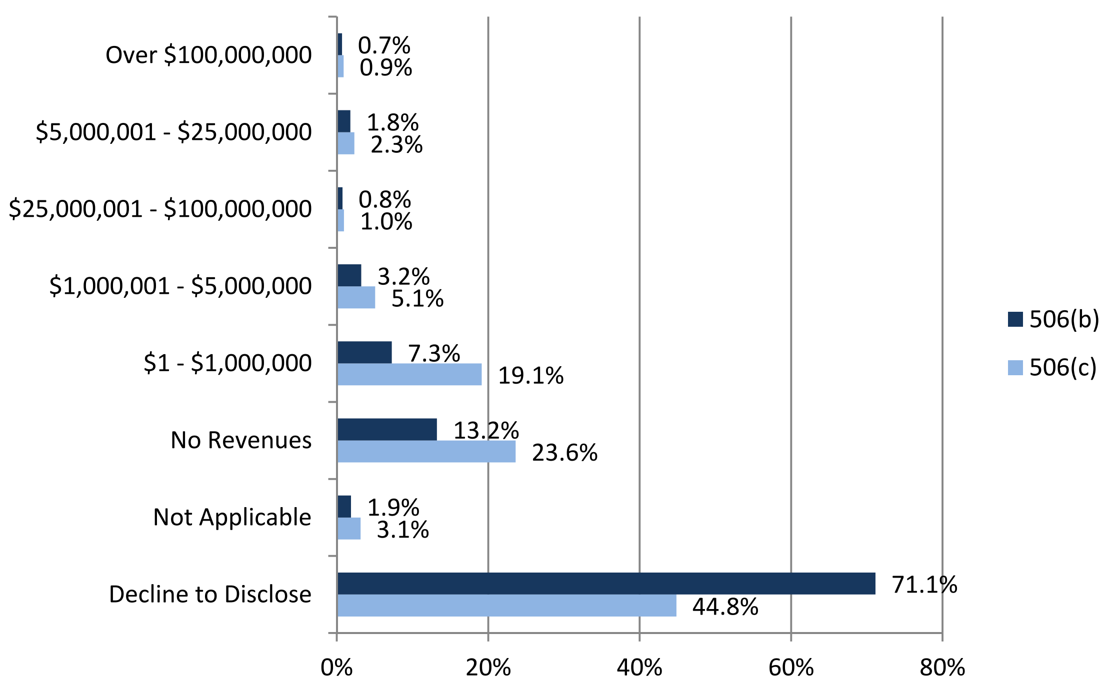
**Figure 14.** Most active non-fund issuers by number of offerings: 2009 -2017



### iv. Issuer Size, Age and Location

Issuer revenue ranges reported in Figure 15 show that issuers of Regulation D offerings tend to be small. Although a significant number of issuers decline to disclose their revenues (71%), for those that do, most have revenues of less than $1 million. Only about 1% of all new offerings are conducted by issuers that report more than $100 million in revenues.[46] By way of comparison, 62% of Exchange Act reporting companies with publicly traded equity report revenues of greater than $100 million at the end of 2016 fiscal year,[47] evidence that issuers seeking capital through Regulation D offerings are significantly smaller than the average publicly traded company.

**Figure 15**. Distribution of non-fund issuers by reported revenue: 2009-2017



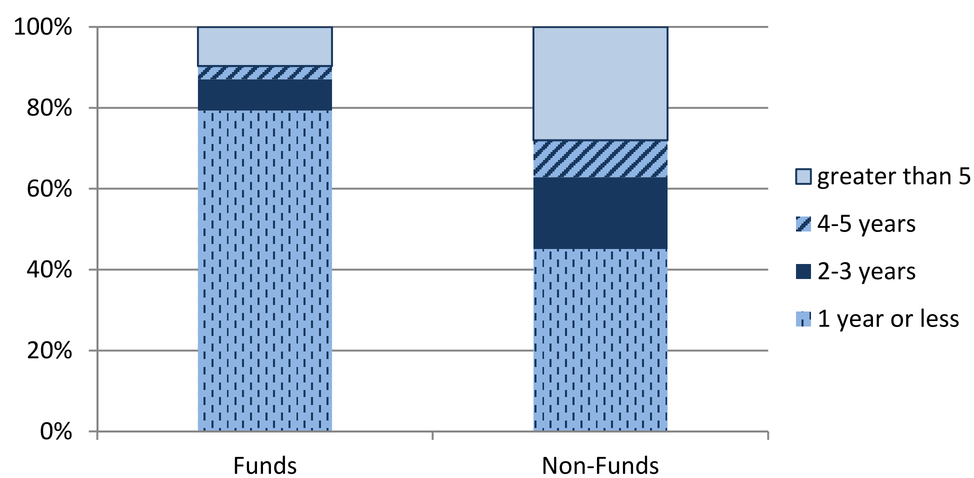

[46] Form D also contains information on net asset value (NAV) of hedge funds and other investment funds. Since 2009, more than three-quarters of issuers have declined to disclose NAV, but of those that do, a trend similar to revenue is reported – the largest set of issuers is in the smallest NAV categories.

[47] Calculated based on DERA analysis of 7,392 SEC registrants who had a class of equity security with a market price reported by Standard and Poor's' Compustat database at the end of fiscal year 2016.

A much smaller proportion of Rule 506(c) non-fund issuers (45%) declined to disclose their size. Of those that did report their size, almost 80% (Figure 15) were either start-up firms (no revenues) or small, early-stage firms ($1-$1million revenue range). The predominance of small issuers indicates that Regulation D, and especially Rule 506(c) capital markets, are active avenues for small business capital formation. Most fund issuers decline to disclose their size when they raise capital in the Rule 506 market. This includes issuers of 68% of all new fund offerings in Rule 506(c) market and almost 91% of new offerings by funds in Rule 506(b) market during the period September 23, 2013 - December 31, 2016.

The small size of Regulation D issuers is also consistent with their younger age, as measured by years since incorporation. 70% of Regulation D issuers were incorporated for less than 3 years when they initiated their offering.[48] This includes 87% of fund issuers and 63% of non-fund issuers (Figure 16). Rule 506(c) issuers, are on average, even younger than Rule 506(b) issuers. 78% of Rule 506(c) issuers, including 75% of non-fund issuers, initiated an offering that permits advertising within 2 years of incorporation.

**Figure 16.** Regulation D issuer age since incorporation: 2009-2017

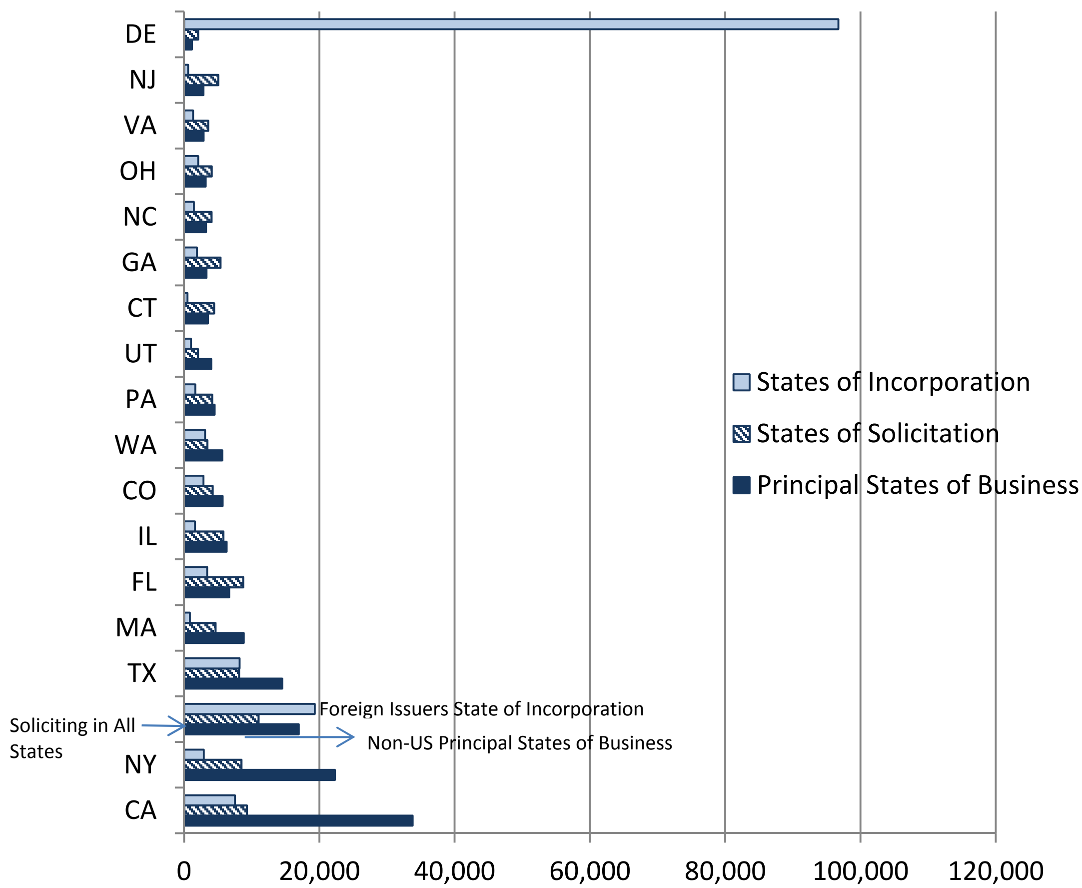



Most Regulation D issuers are located, in terms of principal place of business, in California and New York, even though approximately 54% are incorporated in Delaware (Figure 17). The next largest number of issuers report their principal place of business in Texas, Florida and Massachussetts. 11% of offerings were initiated by foreign incorporated firms. Of those offerings that provide information regarding states of solicitation, the largest number indicate

[48] This includes 0.5-1% of offerings that are yet to be formed. These filings do not report year of incorporation or indicate that they are more than 5 years old.

they are soliciting investors in all U.S. states. Other major states of solicitation are similar in their ordering as the major states of issuer location.

**Figure 17. Issuer state of solicitation, incorporation and primary place of business: 2009-2017**




Similar to Rule 506(b) issuers, most Rule 506(c) issuers report their principal place of business in the states of California, New York, Texas, Florida and Illinois. Approximately 8% of Rule 506(c) offerings were initiated by firms that had their primary place of business outside the U.S., relative to 10% in the Rule 506(b) market during the same period. With respect to states of solicitation, approximately 12% of Rule 506(c) offerings who did report their states of solicitation chose to solicit in all U.S. states. In terms of individual states of solicitation, California ranked number one, followed by Florida, New York, Texas, and Illinois.

### v. Issuer offering activity in Regulation D market

Less than a fifth of Regulation D issuers conducted multiple offerings during the 2009-2017 period (Table 10). Most fund issuers (94%) do not appear to have repeat offerings, which is not surprising given that fund offerings are often continuous in nature and tend to be open for multiple years.[49] Amongst pooled investment funds, only 6% of unique fund issuers had repeat offerings. Over 14% of all fund offerings initiated during 2009-2017 were repeat offerings by multiple-issuance fund issuers. Amongst non-fund issuers, almost 25% of issuers had a repeat offering during 2009-2017. Multiple-issuance non-fund issuers accounted for more than one-half of all non-fund offerings initiated during 2009-2017. Amongst the minority of issuers that did conduct multiple offerings, the average wait time between consecutive offerings (from the initial filing date of the first offering to the initial filing date of the subsequent offering) was 8-10 months.

**Table 10.** Frequency of Regulation D offerings by unique issuers: 2009-2017

| | Non-Fund Issuers | | Fund Issuers | | All Regulation D Issuers |
|---|---|---|---|---|---|
| Number of Offerings | Number of Issuers | Proportion | Number of Issuers | Proportion | |
| 1 | 63,113 | 75.3% | 47,452 | 93.9% | 110,565 |
| 2 | 10,334 | 12.3% | 2,495 | 4.9% | 12,829 |
| 3 | 4,458 | 5.3% | 332 | 0.7% | 4,790 |
| 4 | 2,344 | 2.8% | 110 | 0.2% | 2,454 |
| 5 | 1,385 | 1.7% | 43 | 0.1% | 1,428 |
| 6 or more Offerings | 2,168 | 2.6% | 111 | 0.2% | 2,279 |
| **Total: Unique Issuers** | **83,802** | | **50,543** | | **134,345** |

* *Includes new offerings and offerings initiated prior to 2009 but continuing into years 2009 and later.*

Approximately 40% of Regulation D offerings, predominantly non-fund offerings, raise 100% of capital that they seek by the time they file a Form D with the Commission. Since Regulation D issuers are not required to file a Form D upon completion or termination of their offering, the exact duration of *all* the offerings is not known. But the approximate duration can be estimated from information provided in their filings with the Commission. One such information item requires issuers to state if they expect the duration of their offering to be less than or more than a year. During the period 2009-2017, approximately 54% of Regulation D

[49] We identify unique issuer by their CIK. It is not uncommon that a number of funds that belong to the same family have different CIKs and are therefore identified as separate issuers. From this perspective, the data likely overestimates the number of unique fund issuers and underestimates the frequency of offerings by a family of funds.

issuers that are funds, 19% of issuers that are financial firms, and 6% of operating firms report in their Form D filing that their offering is expected to stay open beyond a year.

### f. Investors in Regulation D offerings

Regulation D allows both accredited and non-accredited investors to participate in private offerings, with an unlimited number of non-accredited investors in Rule 504 offerings, while non-accredited investors are limited to maximum of 35 for Rule 505 and Rule 506(b) offerings. Only accredited investors can participate in Rule 506(c) offerings. Based on information collected from Form D filings, most participants are accredited. For example, during the period 2009-2017, approximately 9% of new offerings included non-accredited investors (Table 11). Offerings by financial issuers and REITs are more likely to have non-accredited investors (12% and 13% of offerings had at least one such investor during 2009-2017), while offerings by VC funds only rarely include non-accredited investors (only 1% of offerings have at least one such investor).

Aggregated Form D information also reveals that during the period 2009-2017 on average approximately 316,288 investors participated in Regulation D offerings, of which about 115,000 participated in offerings by non-financial issuers, more than triple the number of investors that participated in offerings by hedge funds. However, because an investor can participate in more than one Regulation D offering, this aggregation likely overstates the actual number of unique investors, and we have no method of estimating the extent of overlap. The mean number of investors per offering (14) is significantly larger than the median (4), indicating the presence of a small number of offerings with a large number of investors. Offerings by pooled investment funds and REITs have the largest average number of investors (both accredited and non-accredited) per offering, while those by non-financial issuers have the smallest.

**Table 11.** Investors participating in Regulation D offerings: 2009-2017

| | Total Number of Investors* | Mean Investors per Offering | Median Investors per offering | Fraction of offerings with one or more non-accredited investor |
|---|---|---|---|---|
| Hedge Fund | 35,218 | 17 | 2 | 7% |
| Private Equity Fund | 27,174 | 18 | 3 | 4% |
| Venture Capital Fund | 9,097 | 15 | 3 | 1% |
| Other Investment Fund | 38,824 | 24 | 6 | 5% |
| Financial Services | 20,868 | 16 | 4 | 12% |
| Real Estate | 69,705 | 26 | 8 | 13% |
| Non-financial Issuers | 115,403 | 9 | 4 | 9% |
| All offerings | 316,288 | 14 | 4 | 9% |

**2009-2017 data is annualized*

Offerings involving non-accredited investors are typically smaller than those that do not involve non-accredited investors. This is evident from data in Table 12 which shows that while the presence of non-accredited investors was large in Rule 505 offerings (40%), where the number of non-accredited investors was limited to 35 and offering limit was $5 million, the proportion is much higher for offerings under Rule 504 (59%) that have access to an unlimited number of non-accredited investors but had an offer limit of $1 million for the duration of the time period covered by this study. Interestingly much fewer Rule 506 offerings (8%), including amongst those that have an offer size of up to $5 million, report selling or intending to sell to a non-accredited investor. The big difference between Rule 506 and other rules under Regulation D is that the former has preemption from state regulation. Thus, while issuers may prefer to raise capital under Rule 506 because of the preemption of state securities laws, non-accredited investors could be attracted more to Rules 504 and 505 markets because of the higher degree of protection they may perceive to get from state oversight. Additionally, Rule 506 provisions, unlike Rule 504 or Rule 505 provisions, require the non-accredited investors to be 'sophisticated,'[50] which could also explain the lower proportion of Rule 506 offerings that sell or intend to sell to non-accredited investors.

**Table 12.** Proportion of Regulation D offerings that sold or intend to sell to non-accredited investors[51]

| | Rule 504 | Rule 505 | Rule 506(b) Offerings <=$5 million | All 506(b) offerings |
|---|---|---|---|---|
| 2009 | 52% | 38% | 10% | 9% |
| 2010 | 54% | 41% | 9% | 8% |
| 2011 | 56% | 42% | 9% | 8% |
| 2012 | 58% | 43% | 9% | 8% |
| 2013 | 61% | 40% | 9% | 8% |
| 2014 | 59% | 36% | 8% | 7% |
| 2015 | 61% | 43% | 7% | 6% |
| 2016 | 64% | 41% | 6% | 6% |
| 2017 | 66% | 35% | 7% | 6% |
| 2009-2017 | 59% | 40% | 8% | 7% |

Unlike Rule 506(b) offerings that allow accredited investors and up to 35 non-accredited investors, Rule 506(c) allows only accredited investors to participate in advertised offerings. Aggregated Form D information indicates that more than 82,000 investors participated in Rule

[50] Non-accredited investors in Rule 506(b) offerings must have sufficient knowledge and experience in financial and business matters to make them capable of evaluating the merits and risks of the prospective investment. *See* http://www.sec.gov/answers/rule506.htm

[51] Rule 506(c) offerings can sell only to accredited investors.

506(c) offerings since the rule's effectiveness in 2013 (Table 13). Approximately 60% more investors participated in non-fund Rule 506(c) offerings than in fund offerings using general solicitation. The average number of investors per Rule 506(c) offering (12) is smaller than the average number of investors in a Rule 506(b) offering (15). This could be correlated with smaller amount of capital being raised, on average, in a Rule 506(c) offering, relative to a Rule 506(b) offering. But Rule 506(c) offerings by fund issuers have a similar number of investors, on average, as a Rule 506(b) fund offering. The median numbers are similarly much smaller than average number of investors in both Rule 506(c) and Rule 506(b) offerings.

**Table 13**. Investors in Rule 506(c) market: September 23, 2013 - December 31, 2017

| | **Total number of investors** | **Mean investors per offering** | | **Median investors per offering** | |
|---|---|---|---|---|---|
| | All new offerings | All new offerings | New offerings that report investors | All new offerings | New offerings that report investors |
| Rule 506(c) | 82,302 | 12 | 18 | 2 | 7 |
| Funds | 29,681 | 19 | 28 | 4 | 15 |
| Non-Funds | 52,621 | 9 | 16 | 1 | 5 |
| Rule 506(b) | 1,298,470 | 15 | 18 | 4 | 7 |
| Funds | 432,988 | 17 | 25 | 3 | 8 |
| Non-Funds | 865,482 | 14 | 16 | 5 | 6 |

### g. The Role of Financial Intermediaries in the Regulation D market

While financial intermediaries commonly underwrite public offerings, there is relatively little information about intermediary participation in private offerings. One possible role for an intermediary in a private offering is to help issuers locate potential investors without violating the ban on general solicitation, a constraint of the traditional Rule 506 offerings. Using a pre-existing and substantive relationship between the intermediary and potential investors is one method for the issuer to ensure that there was no general solicitation and preserve the Rule 506(b) safe harbor.

Information collected from Form D filings reveals that intermediaries are used relatively infrequently in the Regulation D market. Only about 21% of new offerings by fund issuers during the period 2009-2017 use an intermediary such as a finder or broker-dealer (Table 14), while for non-fund issuers use an intermediary in approximately 20% of new offerings.[52] The data in Table 11 suggests a time trend in the use of intermediaries. Both fund and non-fund issuers experienced a decrease in the use of intermediaries from 2009 to 2017. For example, the use of intermediaries by non-fund issuers declined from approximately 23% in 2009 to approximately 19% in 2017.

**Table 14.** Use of financial intermediaries and average total fees paid by year, 2009-2017.

| | Use of Financial Intermediaries | | Average Total Fees paid | |
|---|---|---|---|---|
| Year | Fund | Non-Fund | Fund | Non-Fund |
| 2009 | 21.4% | 23.3% | 2.5% | 5.8% |
| 2010 | 22.3% | 22.6% | 2.4% | 5.6% |
| 2011 | 24.3% | 21.1% | 2.0% | 5.5% |
| 2012 | 20.4% | 19.9% | 2.0% | 5.6% |
| 2013 | 22.7% | 19.9% | 2.2% | 5.5% |
| 2014 | 18.8% | 18.6% | 1.6% | 5.5% |
| 2015 | 19.7% | 18.6% | 1.5% | 5.2% |
| 2016 | 19.0% | 18.9% | 2.1% | 5.2% |
| 2017 | 21.1% | 19.3% | 2.4% | 5.5% |
| 2009-2017 | 20.9% | 20.0% | 2.1% | 5.5% |

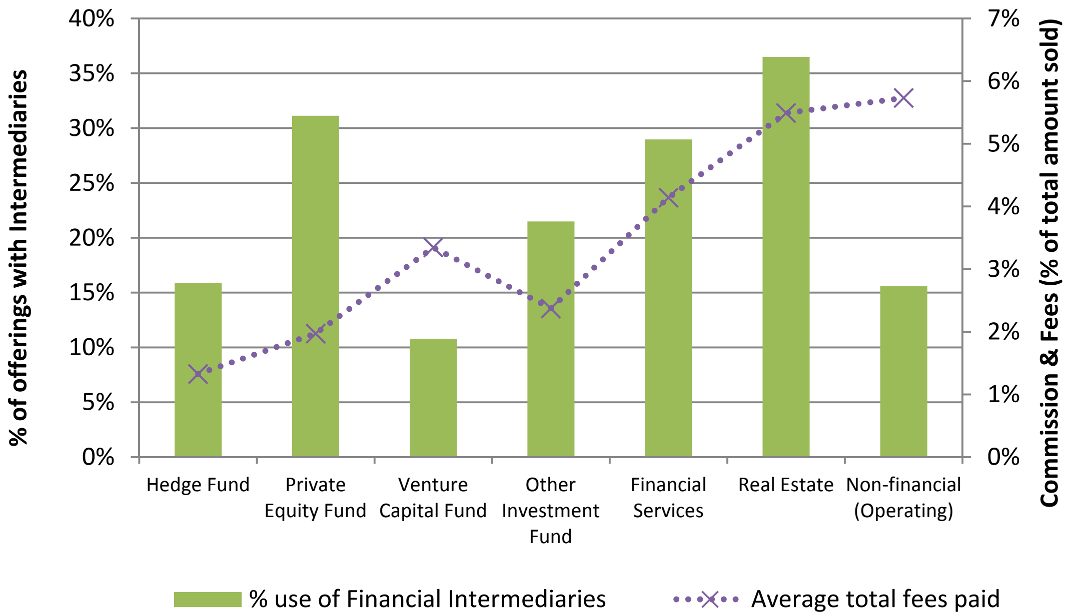
When an intermediary is used, there is significant variation in the fees between fund and non-fund issuers. We calculate the total fee for an offering as the sum of commission and finder's fees, scaled by the offering amount. Information from Form D filings reveals that the total fee paid by fund issuers is on average approximately 2% during the covered period (Table 14). On the other hand, non-fund issuers pay more than twice that amount: their average fee is approximately 5.5%. Differences in offering and issuer characteristics most likely account for the significant difference.

The use of intermediaries also varies significantly by issuer type (Figure 18). Issuers from the real estate industry are the biggest users of intermediaries (37% of all offerings during 2009-2017) while venture capital funds use intermediaries the least (11% of all offerings during 2009-2017). There is also significant usage of intermediaries by private equity funds and

[52] To identify the presence of an intermediary in an offering, we identify those offerings that report paying a commission and/or finder's fee. We also include cases where the CRD number of a recipient of sales compensation is reported on Form D, but no commission and/or finder's fee is paid as of the filing date of the form. Since the issuer could list intermediaries which *will be paid* compensation, we believe that including these cases accounts more accurately for the participation of intermediaries. When calculating the fees paid, however, we only included offerings with positive commission and/or finder's fee.

financial services issuers. Non-financial issuers appear to use intermediaries as frequently as hedge funds (both in about 16% of the offerings).

**Figure 18**. Use of financial intermediaries and fees paid by type of Regulation D issuer: 2009-2017




There is significant variation in the fees across each class of issuers, non-financial issuers paid on average about 6.0% total fee in Regulation D offerings in 2009-2017. For comparison, a company going public pays an average gross spread of 7% to its IPO underwriters,[53] while a public company raising equity through a follow-on (seasoned) equity offering pays a gross spread of about 5.4%.[54] Issuers raising capital through registered bond issues pay commissions between 0.9% and 1.5% of the size of the offering.[55] Crowdfunding issuers pay on average approximately 5% (6% for completed offerings).

In contrast to operating firms, hedge funds raising capital through Regulation D offerings paid about 1%. Like hedge funds, private equity funds enjoy lower fees – on average about 2%. The fees paid by real estate and financial firms are much higher than those paid by fund issuers. Generally, brokers and finders are no more costly, on average, than the underwriting fees

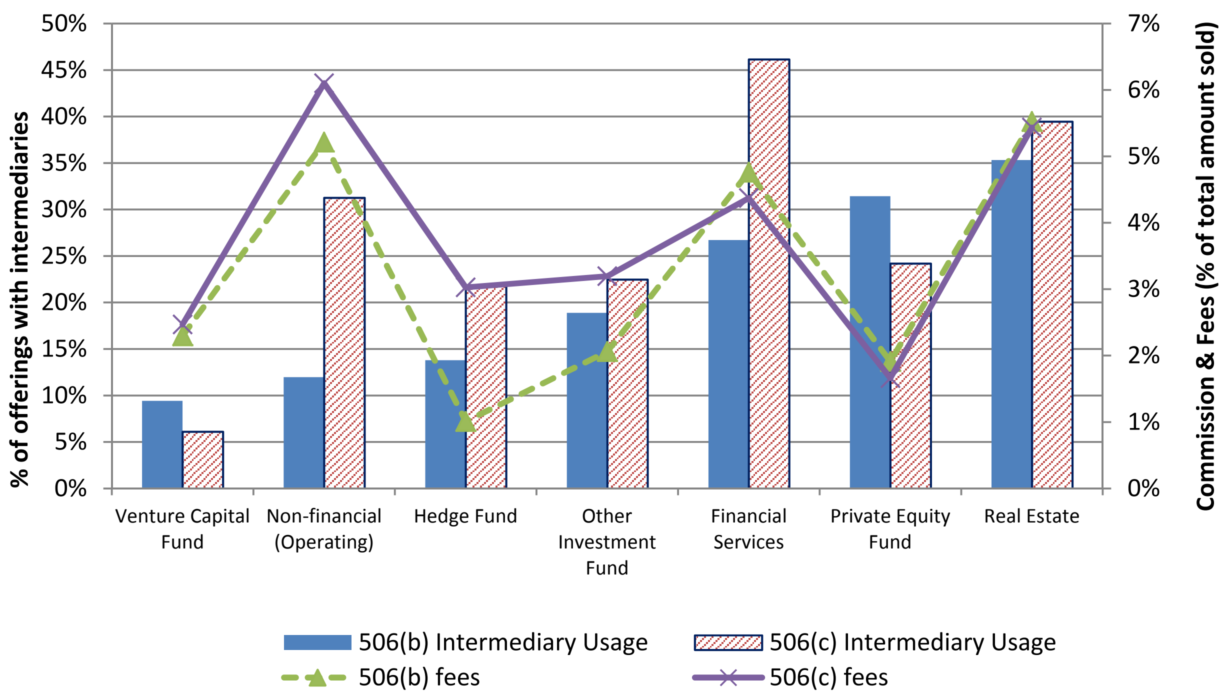
[53] *See* Hsuan-Chi Chen and Jay Ritter, *The Seven Percent Solution*, Journal of Finance 55, 1105-1131 (2000).
[54] *See* Shane Corwin, *The Determinants of Underpricing for Seasoned Equity Offers*, Journal of Finance 58, 2249-2279 (2000).
[55] *See* L. Fang, *Investment Bank Reputation and the Price and Quality of Underwriting Services*, Journal of Finance 60, 2729-2761 (2005).

charged for public offerings,[56] so fees do not provide an obvious reason for their relatively infrequent use in unregistered offerings.

With general solicitation available under new Rule 506(c), it is interesting to see if the role of intermediaries is different from their role in the traditional offerings under Regulation D. Between September 23, 2013-December 31, 2017, intermediary usage in Rule 506(c) offerings was dramatically higher amongst issuers that are operating firms and financial issuers, than similar Rule 506(b) issuers (Figure 19). Overall, Rule 506(c) offerings exhibited a higher level of intermediary usage (32% of new offerings) than Rule 506(b) offerings (18% of new offerings). The higher usage of intermediaries in Rule 506(c) offerings is not entirely surprising because issuers, and especially non-fund issuers, may be relying on outside entities, including third-party online platforms, for the offer and sale of securities and verification of accredited investor status, a requirement for using general solicitation.

On average, Rule 506(c) offerings also pay higher fees (5.4%) than Rule 506(b) issuers (4.6%). Figure 19 shows that operating firms paid almost 6.1% in fees in 506(c) offerings, relative to 5.2% paid by such non-fund, non-financial Rule 506(b) offerings.

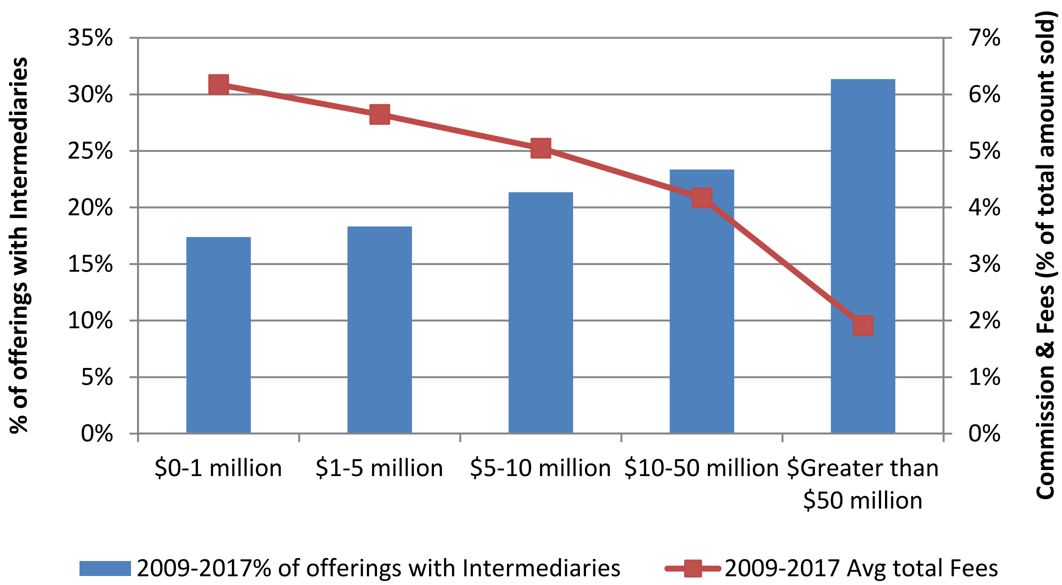
**Figure 19.** Role of intermediaries in Rule 506 market: September 23, 2013 - December 31, 2017




[56] *See* notes 50 and 51.

Figure 20 reports the use of financial intermediaries and fees for different offering sizes, irrespective of issuer type or exemption under Regulation D. The use of a broker or finder increases with offering size; they participate in about 17% of offerings for up to $1 million and 31% of offerings for more than $50 million. Moreover, the total fee decreases with offering size. Unlike the gross spreads in registered offerings, the differences in commissions for Regulation D offerings of different sizes are large: the average commission paid by issuers doing offerings of up to $1 million (6.2%) is more than three times larger than of the average commission paid by issuers doing offerings of more than $50 million (1.9%). These results are consistent with larger deals generating scale economies for the involved intermediaries. Even so, the vast majority of the offerings are conducted without the use of a financial intermediary.

**Figure 20**. Use of financial intermediaries and fees paid by size of Regulation D offering: 2009-2017




## V. Regulation D compared with Other JOBS Act Offering Exemptions

In addition to Title II, the JOBS Act made two other changes to securities offerings regulations: it amended Regulation A and introduced a brand new exemption from registration – Regulation Crowdfunding. Additionally, the Commission amended the intrastate exemptive framework and created new Securities Act Rule 147A to permit companies to generally solicit investors without regard to the location of the investor so long as all purchasers are residents of the same state where the issuer does business. These changes to the exempted securities offerings landscape could have an impact on the use of Regulation D. For example, certain issuers could switch from Regulation D offerings to Regulation A and crowdfunding offerings, thus leaving capital formation unchanged. On the other hand, the changes brought about by Title III and IV of the JOBS Act could bring new issuers to the private offerings market, which would increase capital formation.

#### a. Regulation A and Regulation Crowdfunding

Regulation A is an exemption from registration under Section 3(b)(2) of the Securities Act. Prior to June 19, 2015, it enabled issuers to raise up to $5 million in a 12-month period (subsequently, up to $50 million). It is available to issuers organized, and with a principal place of business, in the United States or Canada. Historically, the Regulation A exemption was not available to Securities Exchange Act of 1934 (Exchange Act) reporting companies, investment companies (including business development companies), development stage companies that have no specific business plan or purpose or have indicated that their business plan is to engage in a merger or acquisition with an unidentified company or companies, issuers of fractional undivided interests in oil or gas rights or a similar interest in other mineral rights. In addition, Regulation A also excludes issuers that have not filed certain ongoing reports required by Regulation A, issuers subject to certain Section 12(j) orders by the Commission, and issuers subject to "bad actor" disqualification under Rule 262.

Title IV of the JOBS Act added Section 3(b)(2) to the Securities Act, directing the Commission to adopt rules exempting from registration public offerings of up to $50 million annually. On March 25, 2015, the Commission adopted final rules.[57] The final rules expand Regulation A into two tiers: Tier 1, for securities offerings of up to $20 million (that tracks more closely "old" Regulation A); and Tier 2, for offerings of up to $50 million. Under the final rules, Tier 2 issuers are required to include audited financial statements in their offering documents and to file annual, semiannual, and current reports with the Commission. With the exception of securities listed on a national securities exchange, purchasers in Tier 2 offerings either must be accredited investors or are subject to specified limitations on their investment. The amendments to Regulation A became effective on June 19, 2015.

Title III of the JOBS Act (Regulation Crowdfunding) amended Section 4 of the Securities Act and created a new exemption from registration for Internet-based securities offerings of up to $1 million[58] over a 12-month period. Title III was intended to help small and startup businesses conduct low-dollar capital raising on the Internet. It can be thought of as an

[57] *See* Amendments to Regulation A, SEC Release No. 33-9741 (March 25, 2015) [80 FR 21805 (April 20, 2015)], *available at* http://www.sec.gov/rules/final/2015/33-9741.pdf.
[58] *See* SEC Releases No. 33-9974 (Oct. 30, 2015) [80 FR 71387 (Nov. 16, 2015)] (Crowdfunding Adopting Release), *available at* https://www.sec.gov/rules/final/2015/33-9974.pdf.. On March 31, 2017, the Commission adopted amendments to increase the amount that issuers can raise through crowdfunding to adjust for inflation. The maximum aggregate offering amount increased to $1,070,000, and the new thresholds became effective on April 12, 2017.

Internet-based method of raising seed financing from a broad, mostly retail investor base. Title III included a number of investor protection provisions, including investment limitations, issuer disclosure requirements, and a requirement to use regulated intermediaries. The SEC adopted the final "Regulation Crowdfunding" rules on October 30, 2015, to implement the requirements of Title III.[59] Issuers were able to use the new exemption beginning May 16, 2016, when Regulation Crowdfunding became fully effective.[60]

While securities-based crowdfunding under Regulation Crowdfunding shares certain similarities with non-securities-based (lending-based, reward-based, donation-based, and royalty-based) crowdfunding, such as the ability of the public to participate and the use of an Internet-based platform to solicit backers, there are important distinctions. Non-securities-based crowdfunding campaigns do not involve a profit or revenue-sharing model and are generally not subject to regulation under federal securities laws. Although any crowdfunding backer may have nonpecuniary reasons for participating, backers in non-securities based crowdfunding campaigns are more likely to be guided by such motives. Overall, the differences in the legal framework, characteristics of fundraisers, and objectives of funders limit extrapolation from non-securities based crowdfunding to Title III crowdfunding.

Regulation Crowdfunding established requirements for issuers and intermediaries seeking to participate in an Internet-based crowdfunding offering. The key provisions are summarized below:[61]

- A given issuer is able to raise up to $1,070,000 across all crowdfunding offerings in a 12-month period. An issuer must raise at least the target amount to receive funds. Crowdfunding securities are generally subject to resale limitations for one year.
- The rules impose limits on the amount that an investor can invest in all Title III crowdfunding offerings over a 12-month period. Investors with both an annual income and net worth of at least $107,000 can invest up to 10% of the lesser of annual income or net worth, but an investor's total investment across all Title III offerings may not exceed $107,000 in a 12-month period. Other investors can invest the greater of either $2,200 or 5% of the lesser of their annual income or net worth.
- Crowdfunding issuers are subject to disclosure requirements at the time of the offering (on Form C), during the offering's progress and on completion of the offering (on Form C-U) and annually in the form of annual reporting requirements (on Form C-AR). Additionally, in offerings of over $107,000 in a 12-month period, financial statements

[59] *See* Crowdfunding Adopting Release.
[60] Provisions related to funding portal registration became effective on January 29, 2016, to give funding portals additional time to undergo the SEC registration and FINRA membership process.
[61] *See* Crowdfunding Adopting Release for details. In the JOBS Act Technical Amendments Release, the Commission revised the investment limits and other dollar amount thresholds in Regulation Crowdfunding to adjust for inflation. The inflated-adjusted amounts are reflected below.

must be reviewed by an independent accountant, and in offerings of over $535,000 in a 12-month period (except the issuer's first crowdfunding offering), financial statements must be audited.

- Crowdfunding securities must be offered through an SEC-registered intermediary, either a broker-dealer or a funding portal, a new intermediary type established in Regulation Crowdfunding. These intermediaries must take measures to reduce the risk of fraud, make required disclosures about issuers available to the public, provide communication channels to permit discussion of offerings on the platform, disclose the compensation received by an intermediary, provide educational materials to investors, and comply with additional requirements related to investor commitments, notices to investors, and maintenance and transmission of funds. Registered funding portals that participate in crowdfunding offerings may engage in a narrower set of activities than broker-dealers.[62]

Given the offering limits, crowdfunding is primarily used by relatively small issuers, thus many of the economic considerations applicable to small and early-stage issuers apply to crowdfunding as well.[63] The availability of solicitation over the Internet and sales to investors nationwide, irrespective of the location of the issuer (as long as the issuer is a U.S. issuer) distinguish Regulation Crowdfunding from intrastate securities-based crowdfunding regulated under state law that historically has relied on Securities Act Rules 147 or 504.[64]

#### b. Comparison between Regulation D offering and Regulation A and Regulation Crowdfunding offerings

Compared to Regulation Crowdfunding offerings, Regulation D offerings for up to $1 million are more numerous and raise significantly more capital (Table 15). Regulation D issuers also tend to be younger (approximately 55%% are less than a year old at the time of the offering). On the other hand, issuers relying on Regulation Crowdfunding tend to be smaller as based on the size of their revenues, although caution is due when making such comparison given that about 70% of Regulation D issuers declined to disclose their revenues.

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[62] Among other things, a funding portal cannot offer investment advice or recommendations; solicit purchases, sales or offers to buy the securities offered or displayed on its platform; compensate employees, agents or other persons for solicitation or based on the sale of securities on its platform; and hold, manage, possess, or otherwise handle investor funds or securities.

[63] *See* Crowdfunding Adopting Release.

[64] *See* Crowdfunding Adopting Release. The Commission recently amended Rule 147 and Rule 504 and adopted a new intrastate offering exemption as Rule 147A. *See* Rel. No. 33-10238, *Exemptions to Facilitate Intrastate and Regional Securities Offerings* (Oct. 26, 2016). Amendments to Rule 504 took effect on January 20, 2017. The amended Rule 147 and the new Rule 147A took effect on April 20, 2017.

It is notable that very few of the Regulation Crowdfunding issuers have used Regulation D offerings in the past – about 13% undertake a Regulation D offering prior to the Regulation Crowdfunding offering.

**Table 15.** Offerings up to $1 million: Regulation D and Regulation Crowdfunding, May 16, 2016 – December 31, 2017

| | Regulation D | Regulation Crowdfunding |
|---|---|---|
| **Number of offerings** | 11,646 | Ongoing: 643<br>Finished: 205 |
| **Amount raised** | | |
| Total | $3.49 billion | Ongoing – Target amount: 52.6 mil<br>Ongoing – Maximum amount: 378.0 mil<br>Finished: 53.2 mil |
| Mean (Median) ($ mil) | 0.30 (0.19) | Ongoing – Target amount: 0.08 (0.05)<br>Ongoing – Maximum amount: 0.62 (0.55)<br>Finished: 0.26 (0.16) |
| **Issuer revenue distribution** | | |
| $1 - $1 million | 12.4% | 40.2% |
| $1 - $5 million | 2.2% | 5.8% |
| $5 - $25 million | 0.9% | 1.4% |
| $25 - $100 million | 0.3% | 0% |
| Over $100 million | 0.2% | 0% |
| No Revenues | 15.2% | 52.6% |
| Decline to Disclose | 66.4% | |
| Not Applicable | 2.6% | |
| **Issuer years since incorporation** | | |
| 1 year or less | 50% | 2% |
| 2-3 years | 17% | 47.1% |
| 4-5 years | 7.6% | 33.4% |
| Greater than 5 | 25.4% | 17.5% |

Table 16 compares Regulation D and Regulation A offerings. When compared to Tier 1 and Tier 2 Regulation A offerings, Regulation D offerings of similar sizes are more numerous and raise significantly more capital in the aggregate across all offerings. On average, Tier 1 offerings tend to be larger than the average size of Regulation D offerings of up to $20 million, while Tier 2 offerings have similar average offering size as their corresponding Regulation D offerings. There is also significant difference in the industry distribution of issuers between Regulation D and Regulation A offerings, with a large percentage of Regulation A issuers coming from Business Services, Commercial Banking, and Investing.

**Table 16.** Regulation D and Regulation A: Offerings for up to $20 million and up to $50 million, May 16, 2016 – December 31, 2017

| | **Regulation D**<br>Up to $20 million | **Regulation A**<br>Tier 1 | **Regulation D**<br>Up to $50 million | **Regulation A**<br>Tier 2 |
|---|---|---|---|---|
| **Number of offerings** | 29,389 | Qualified offerings: 57<br>Finished offerings: 17 | 32,265 | Qualified offerings: 128<br>Finished offerings: 61 |
| **Amount raised** | | | | |
| Total | $98.5 billion | Amount sought: $488.1 million<br>Amount raised: $126.0 million | $204 billion | Amount sought:$3.7 billion<br>Amount raised: $542.7 million |
| Mean (Median) ($ million) | 2.7 (1) | Qualified offerings:8.6 (5.0)<br>Finished offerings: 7.4 (4.5) | 4.6 (1.1) | Qualified offerings: 28.6 (25.0)<br>Finished offerings: 8.9 (3.5) |
| **Five main industries** | | | | |
| | Pooled Investment Fund (30.3%) | Business Services (19.3%) | Pooled Investment Fund (34.1%) | Investing (13.6%) |
| | Other Technology (15.8%) | Depositary Institutions (19.3%) | Other Technology (14.6%) | Real Estate (12.8%) |
| | Other (14.7%) | Non-depositary Credit Institutions (12.3%) | Other (13.5%) | Business Services (12.0%) |
| | Commercial (5.2%) | Real Estate (10.5%) | Commercial (4.9%) | Transportation Equipment (8.8%) |
| | Other Health Care (4.6%) | Motion Pictures (5.3%) | Other Health Care (4.4%) | Non-depositary Credit Institutions (4.8%) |

# Appendix I: Data Used in Analysis

This appendix describes the procedures used to collect the Regulation D sample and the data on the other offerings. One of the original purposes of Form D, first adopted in 1982, was to collect and analyze data on issuers using Regulation D.[65] However, until 2008, issuers filed Form D on paper, making the extraction of information for large-scale statistical analysis cumbersome. In February 2008, the SEC adopted amendments to Form D that required issuers to submit their Form D filings electronically, in a structured data format.[66] As a result of these requirements, which were phased in from September 2008 through March 2009, Form D filings are now machine-readable. Using basic text parsing tools, DERA staff was able to extract the reported elements and place them in a database enabling the large-scale statistical analysis reported here.

## A. Regulation D sample

We collected all Form D filings (new filings and amendments) on EDGAR starting in January 2009 through December 2017. We extracted all fields from each filing and applied the following treatments to arrive at our final sample.

- Subsequent amendments to a new filing are treated as incremental fundraising and recorded in the calendar year in which the amendment is filed. For offerings initiated prior to 2009 and continuing into future years, an issuer would have filed only Form D amendments in an electronic (machine readable) form required for this analysis. If these amendments reference a post-2008 sale date, the first filed amendment is treated as an original Form D filing as we do not have access to Form D data prior to 2009.
- The incremental amount sold between two successive filings of the same issuer is determined by taking the difference between the "total amounts sold" reported in each such filing.
- We estimate the incremental amount of capital raised and reported in amended filings for which there is no original filing in electronic form. This occurs only in 2009. The estimated incremental capital raised in these instances is based on a "haircut" of the total amount sold reported in the latest filed amendment. This percentage is the average incremental amount sold in all amendments for which there is an original filing in electronic form, calculated separately for funds and non-funds. This

[65] Release No. 33–6389 (Mar. 8, 1982); 47 Fed. Reg. 11251 (1982) (adopting Form D as a replacement for Forms 4(6), 146, 240 and 242).
[66] Release No. 33–8891 (Feb. 27, 2008); Electronic Filing and Revision of Form D, 70 Fed. Reg. 10,592 (2008) .

resulted in haircut percentages of 11% and 27%, respectively. This treatment is unnecessary for offerings starting in 2010.

- A number of pooled investment funds appear to report, in their annual amendments, net asset values for total amount sold under the offering. Net asset values could reflect fund performance as well as new investment into, and redemptions from, the fund. Since it is not possible to distinguish between the two impacts, we present the second category of amendments (filed for offerings initiated prior to 2017) separate from the total amount raised in initial offerings. However, it is plausible that amendments filed within the same year when offerings are initiated, would reflect updates to capital raising efforts of the issuers. Therefore, we use the incremental amounts in the first set of amendments in calculating total amount raised in initial offerings.
- Foreign issuers are determined based on the information on Issuer State that they provide.
- When an issuer checks the box to claim more than one offering exemption (Rule 504, 505, or 506), for the purpose of this analysis, we assume that any issuer that checks the box for Rule 506 is in fact relying on Rule 506.

## B. Other offerings

- Data on IPOs, equity offerings by seasoned issuers (EOSIs), convertible debt offerings, public debt offerings, and private offerings are taken from Securities Data Corporation's New Issues database (Thomson Financial). Data on non-ABS Rule 144A offerings are taken from Securities Data Corporation's New Issues database, Dealogic, and Mergent database.
- Data on ABS Rule 144A offerings are taken from the Asset-Backed Alert and Commercial Mortgage Alert publications. We use non-U.S. collateral backed deals to proxy for deals done by foreign issuers.
- Public debt offerings by government, state, municipal, and quasi-governmental issuers (e.g., Fannie Mae, Freddie Mac) are excluded from the public debt sample.

# Appendix II: Federal Exemptions and Safe Harbors for Unregistered Offerings by Issuers*

| Type of Offering | Offering Limit | General Solicitation | Issuer and Investor Requirements | Filing Requirement | Restrictions on Resale | State Securities Law Preemption |
|---|---|---|---|---|---|---|
| **Section 3(a)(11)** | None | No offerees must be resident in state | All issuers and investors must be resident in state. | None | Section 3(a)(11) does not impose resale restrictions, but state securities laws may do so. Securities Act Rule 147, a safe harbor under Section 3(a)(11), limits resales to persons residing in-state for a period of nine months after the last sale by the issuer. | No preemption. Need to comply with state laws registration requirements or rely on state exemption. |
| **Section 4(a)(2)** | None | No general solicitation or advertising. | Transactions by an issuer not involving any public offering. All investors must meet sophistication and access to information test so as not to need protection of registration. | None | Restricted securities. | No preemption. Need to comply with state law registration requirements or rely on state exemption. |
| **Regulation A** | Tier 1: $20 million with $6 million limit on secondary sales by affiliates of the issuer, within prior 12 months;<br>Tier 2: $50 million with $15 million limit on secondary sales by affiliates of the issuer, within prior 12 months.. | "Testing the waters" permitted. Sales permitted after Form 1-A qualified. | U.S. or Canadian issuers, excluding investment companies, blank-check companies, reporting companies, and issuers of fractional undivided interests in oil or gas rights, or similar interests in other mineral rights. | File testing the waters materials and Form 1-A for Tiers 1 and 2; file annual, semi-annual, and current reports for Tier 2; file exit report for Tier 1 and to suspend or terminate reporting for Tier 2 | None; freely resalable. | Tier 1: No preemption, offerings need to comply with state laws.<br>Tier 2: Offerings have state law pre-emption. |

| Type of Offering | Offering Limit | General Solicitation | Issuer and Investor Requirements | Filing Requirement | Restrictions on Resale | State Securities Law Preemption |
|---|---|---|---|---|---|---|
| **Regulation S** | None | Available only for offer and sale of securities outside the United States. None of the parties can make any "directed selling efforts" in the United States. | Issuers cannot be open-end investment companies or those registered under Investment Company Act of 1940, or closed-end investment companies required to be registered, but not registered, under the 1940 Act.<br>Can be foreign investors or U.S. investors who enter foreign markets, subject to limitations. | None | Restricted during distribution compliance period; subsequent resale transaction has to be registered under Securities Act or be exempt from registration. | No preemption. Also need to comply with registration requirements in countries/exchanges where offer is made. |
| **Rule 504 Regulation D** | As amended, $5 million within prior 12 months. | No general solicitation or advertising unless registered in a state requiring use of a substantive disclosure document or sold under state exemption for sales to accredited investors with general solicitation. | Excludes investment companies, blank-check companies, and Exchange Act reporting companies. | File Form D. Filing not a condition of the exemption. | Restricted unless registered in a state requiring use of a substantive disclosure document or sold under state exemption for sale to accredited investors with general solicitation. | No preemption. Need to comply with state law registrations requirements or rely on state exemption. |

| Type of Offering | Offering Limit | General Solicitation | Issuer and Investor Requirements | Filing Requirement | Restrictions on Resale | State Securities Law Preemption |
|---|---|---|---|---|---|---|
| **Rule 505 Regulation D (Repealed, effective May 20, 2017** | $5 million within prior 12 months. | No general solicitation or advertising. | Unlimited accredited investors and 35 non-accredited investors. | File Form D. Filing not a condition of the exemption. | Restricted securities | No preemption. Need to comply with state law registration requirements or rely on state exemption. |
| **Rule 506(b) Regulation D** | None | No general solicitation or advertising | Unlimited number of accredited investors and 35 non-accredited investors that are sophisticated. | File Form D. Filing not a condition of the exemption. | Restricted securities | Yes . |
| **Rule 506(c) Regulation D** | None | General solicitation and general advertising permitted, provided that all purchasers are accredited investors and the issuer takes reasonable steps to verify accredited investor status. | All purchasers must be verified to be accredited investors. Unlimited number of accredited investors. | File Form D. Filing not a condition of the exemption. | Restricted securities | Yes. |

*This is only a summary of certain requirements contained in the Commission's rules and regulations; it is not a substitute for the rules and regulations.