

H.R. 79, Section 452 of H.R. 10, and Section 913 of H.R. 3280: Helping Angels Lead Our Startups

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The Jumpstart Our Business Startups Act of 2012 (JOBS Act; P.L. 112-106) was broadly aimed at stimulating corporate capital formation, particularly for emerging and smaller firms, largely through regulatory relief from various disclosure-based requirements in federal securities laws administered by the Securities and Exchange Commission (SEC).

In recent years, Congress has considered legislation extending the JOBS Act's focus on corporate regulatory relief. In the 115th Congress, such legislation includes H.R. 79, Helping Angels Lead Our Startups, which passed the House on January 10, 2017. Identical language was also included in Section 452 (Helping Angels Lead Our Startups) of H.R. 10, the Financial CHOICE Act, which passed the House on June 8, 2017, and Section 913 (Helping Angels Lead Our Startups) of H.R. 3280, the Financial Services and General Government Appropriations Act, 2018, which was marked up by the House Committee on Appropriations on July 18, 2017. Policy issues related to these proposals are examined in this Insight.

Demo Days and Rule 506

Prospective corporate issuers often find it useful to market their private offerings at promotional events known alternatively as demo days, venture fairs, or pitch days (generically often called demo days). The events are often sponsored by angel investors (wealthy nonprofessional investors), venture capital associations, nonprofits, or universities and are used to communicate that a company is interested in, if not actively seeking, investor financing.

Rule 506 of Regulation D (Reg D) under the Securities Act of 1933 permits companies to offer privately placed (through private markets) equity or debt securities offerings to any number of accredited investors (financial institutions and individual investors who meet certain asset or income thresholds) (and up to 35 nonaccredited investors) without being subject to state and federal securities registration requirements. Popular with emerging companies, Rule 506 offerings have no size limits but were historically subject to a general solicitation ban (a prohibition on their general promotion or advertising). In response to concerns that the ban was both antiquated and burdensome, the JOBS Act amended Rule 506 by creating

an offering category under Reg D called Rule 506(c), wherein issuers are allowed to engage in general solicitations to accredited investors while taking “reasonable steps” to verify their accredited status.

After Rule 506(c)’s adoption, there was uncertainty over whether issuers were still subject to the ban on general solicitation at demo days. An August 2015 [SEC question and answer guidance document](#) attempted to provide some clarity. It reported that if prospective investors were invited to a demo day by an issuer or a person acting on its behalf via a general solicitation, the issuer may then be able to use Rule 506(c) if it takes reasonable steps to verify that a purchaser is an accredited investor and that the offering is limited to such investors.

Notwithstanding the SEC guidance, uncertainty over the applicability of the general solicitation ban at demo days persisted. In addition, other concerns existed that even if the general solicitation ban was clearly not being enforced at demo days, the demands of the accredited investor verification process would discourage investor interest.

H.R. 79, Section 452 of H.R. 10, and Section 913 of H.R. 3280

H.R. 79, Section 452 of H.R. 10, and Section 913 of H.R. 3280 attempt to address concerns related to demo days. They would require the SEC to revise Rule 506 of Reg D to clarify that the limits on general solicitation are not applicable to presentations, communications, or events conducted on behalf of an issuer at an event sponsored by certain organizations, including (1) the United States or any territory thereof, the District of Columbia, or any state; (2) a college, university, or other institution of higher education; (3) a nonprofit organization; (4) an angel investor group; (5) a venture forum, venture capital association, or venture capital trade association; or (6) any other group, person, or entity that the SEC may designate.

In addition, advertising for such an event cannot reference any specific offering of securities by the issuer, and no specific information on a securities offering by an issuer can be communicated or distributed by or on behalf of the issuer.

Introduced in the 114th Congress, H.R. 4498, identical to the legislation in the 115th Congress, earned the support of various business trade groups, including the [U.S. Chamber of Commerce](#). An angel investor trade group, [the Angel Capital Association](#), [reported](#) that the bill would eliminate the burdens and uncertainties inherent in current SEC policy on issuers with respect to general solicitations during demo days by removing demo days from the restrictions on general solicitation. It also noted that although demo days are public events, investors with an interest in acquiring a stake in a new company would still be required to be accredited investors. Similarly, the Chamber of Commerce [claimed](#) that the bill would improve the information flow on the market for start-ups, helping to broaden angel investor interest in early-stage corporate investments.

However, critics of the earlier bill, including a pro-regulatory reform group, [Americans for Financial Reform](#), said that the bill raised investor protection concerns. In this context, a [statement on the bill from the White House](#) observed that H.R. 4498 did not adequately “weigh the need for, and importance of, appropriate investor protections.” In [testimony](#) that expanded on these concerns, Professor Joseph Carcello, a university accounting professor, said that H.R. 4498’s extension of public demo day sponsors to governmental entities, nonprofits, and colleges would invite participation from investors who would not necessarily be accredited investors and could thus lack adequate financial sophistication and the financial wherewithal needed to weather a bad investment decision. This was particularly concerning, he said, because the legislation would have done away with the Rule 506(c) requirement that an issuer must take reasonable steps to verify an investor’s accredited investor status for sales events like demo days.

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