Securities Regulation and Social Media

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Federal securities regulation originally divided corporate finance into two neat categories, public and private. In 1933, private financing was limited to "sophisticated" investors but otherwise lightly regulated. Public financing became heavily regulated. In 1982, the SEC introduced Reg D, which introduced the concept of "general solicitation" to clarify the distinction between public and private offerings. Reg D is well understood to prohibit newspaper advertisements and permit direct solicitations to venture capital investors. This enabled great wealth consolidation in regions like Silicon Valley while effectively banning general solicitations in private offerings.

Now, social media communication challenges the definition of "general solicitation." Although social media comes in a multitude of forms, there is no guidance as to whether a single post or tweet might violate securities regulations. Confusion and fear of violating the ban on general solicitation chills online investment, even though online investment technology offers new and better means of protecting investors from fraud and undue risk.

Meanwhile, society has grown wary of regulations that tend to concentrate immense wealth amid a privileged few. Movements like Occupy Wall Street demanded that ordinary Americans gain equal access to financial markets, and legislators adopted equal access to capital as the national entrepreneurship policy.

In today's interconnected age, the general solicitation ban has a disparate impact on young, rural, poor, and otherwise less established entrepreneurs. It systematically advantages established, urban, wealthy, and other well-connected businesspeople. The unintended consequence of the general solicitation ban is a disparate impact upon the members of society who could benefit the most from entrepreneurial opportunities. The general solicitation ban helps the rich and well connected get richer while excluding new entrepreneurs and diverse investors from capital markets. The ban is technologically and socially out of date. Accordingly, the ban carries the heavy burden of proving that it prevents enough fraud to be worth its cost. It

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has not met this heavy burden. Therefore, the general solicitation ban should be abolished.

INTRODUCTION

Startup entrepreneurs' first round of fundraising usually comes from friends and family.[1] The SEC permits such fundraising so long as the entrepreneurship does not "generally solicit"[2] the funds. This rule was relatively clear in an analog age, where a handwritten letter to Grandma was not a general solicitation but an advertisement in the *New York Times* clearly was. But how does this rule apply to the digital age, where social media is the dominant platform for communication?

This question is increasingly relevant today, when nearly one million people become new active social media users every day.[3] Already, almost half of the world's population uses social media. The world's 4.4 billion internet users spend an average of six-and-a-half hours online every day, and three of the top ten most visited websites are social media sites.[4]

More to the point, securities regulations themselves have had a major impact on social media. Dozens of new social media investing platforms have recently emerged in a direct response to the Jumpstart Our Business Startups (JOBS) Act of 2012, which permits new ways to sell securities online.[5] Entirely new industries have formed around "crowdfunding."[6]

Yet a fundamental question remains. Entrepreneurs are still prohibited from raising money from nonaccredited investors via a general solicitation, but what is a general solicitation on social media? This is not just a theoretical question but also a practical one; today's entrepreneurs might think nothing of sharing information about their startup fundraising with friends and family on Facebook, Twitter, or Instagram. Yet improper

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1. Seth C. Oranburg, *Bridgefunding: Crowdfunding and the Market for Entrepreneurial Finance*, 25 CORNELL J. L. & PUB. POL'Y 396, 410 (2015) (explaining how the startup fundraising cycle begins with seed funding, which generally comes from family, friends, and fools).

2. The SEC defines "general solicitation" to include "advertisements published in newspapers and magazines, public websites, communications broadcasted over television and radio, and seminars where attendees have been invited by general solicitation or general advertising. In addition, the use of an unrestricted, and therefore publicly available, website constitutes general solicitation." *Eliminating the Prohibition Against General Solicitation and General Advertising in Rule 506 and Rule 144A Offerings: A Small Entity Compliance Guide*, SEC (Sept. 20, 2013), https://www.sec.gov/info/smallbus/secg/general-solicitation-small-entity-compliance-guide.htm [https://perma.cc/F996-Q83X].

3. Simon Kemp, *Digital 2019: Global Internet Use Accelerates*, WE ARE SOC. (Jan. 31, 2019), https://wearesocial.com/us/blog/2019/01/digital-2019-global-internet-use-accelerates [https://perma.cc/LG5B-4JEY].

4. The third most visited web site is Facebook.com, the sixth most visited site is Twitter.com, and the seventh most visited site is Instragram.com. Martin Armstrong, *The World's Most Popular Websites*, STATISTA (Nov. 25, 2019), https://www.statista.com/chart/17613/most-popular-websites/ [https://perma.cc/88N8-JULR].

5. *See* CROWDFUND Act, 15 U.S.C. § 77d–1 (creating a "crowdfunding" exemption).

6. Crowdfunding is defined as "raising a large amount of money from a large number of people via the internet." Seth C. Oranburg, *Hyperfunding: Regulating Financial Innovations*, 89 U. COLO. L. REV. 1033, 1078 (2018).

use of social media could violate securities regulations, thus making the transaction voidable or even resulting in fines and penalties for startups and entrepreneurs. It also brings up important theoretical issues about the meaning and importance of the ban on general solicitation.

This Article will respond to this fundamental question in several parts. Part I highlights the problem with the general solicitation ban through the story of two entrepreneurs. Part II comprehensively reviews the securities regulations themselves, including the historic ban on general solicitation and recent amendments that allow internet offerings. Part III looks at the new social media investment platforms that have emerged to exploit these new opportunities and the ways in which present law continues to constrain their business models. Part IV examines the technical nature of online social media and attempts to answer the question of whether or when a social media post constitutes a general solicitation under present law. Part V discusses the arguments regarding the general solicitation ban. The Article then briefly concludes on why the ban should be eliminated.

I. An Illustration of the Problem: A Tale of Two Entrepreneurs

The general solicitation ban is counterintuitive and counterproductive in today's social media world. As these fictional illustrations will show, it is far too easy to violate the ban. Moreover, the ban creates a disparate impact against small town entrepreneurs, who, compared to a big city startup, need social media to reach a larger audience. Social media has democratized speech. It also has the power to democratize entrepreneurship. But the ban on general solicitation prevents social media from creating more equal access to entrepreneurship and financial success.

A. The Small-Town Entrepreneur

Karen was a rural success story. She was the one who got away from Dallas, South Dakota—a town so small that its post office closed in 1973.[7] Karen walked thirty minutes each day from her home in Ace's RV Park to Gregory High School. When she graduated in 2013, most of her twenty-four classmates went to work for the local municipal airport,

7. The population of Dallas, South Dakota, was 120 at the 2010 census. While this is an extreme example, small towns are common in America: about 59.5 million people (almost 20% of the national population) live in rural areas. UNITED STATES CENSUS 2010, U.S. CENSUS BUREAU (2010).

waited tables in Mary Bob's Bar[8] or Sissy's Café,[9] or joined the army. But Karen had greater ambitions. She studied hard and won a partial scholarship to the University of South Dakota Beacom School of Business.[10] Throughout school, Karen paid her bills by managing the Nature's Way Juice Bar in nearby Sioux Falls.[11] She earned a Master of Business Administration (MBA) in 2018.

Karen wanted to use her new skills and knowledge to help Dallas become more like its namesake in Texas. She wanted to be near her family, too, so she moved back home and set about starting a new business there. She was determined to open a juice bar so Dallas residents would have a healthy eating option. She found a suitable location and shopped online for all the equipment she would need.

The problem was financing the startup costs. Karen was saddled with debt from student loans and did not have cash in the bank. Her mother was in poor health, out of work, and barely able to afford rent in her trailer park. In fact, Karen didn't know any wealthy people at all. She asked the two banks in Dallas, BankWest and First Fidelity Bank, for a loan, but they refused to lend money to a first-time entrepreneur with no collateral. Karen was frustrated, but she did not give up.

Instead, Karen turned to the internet and reengaged with her Facebook group, Juicing for Life, a juicing support group with 32,000 members.[12] She posted about her dream of creating a healthy juice bar in her tiny hometown, and many members on the Facebook group cheered her on. When Karen complained of the difficulty of fundraising for a new business in a tiny town with a population of less than a hundred people, group members commiserated with her. Then, one day, Jalene, the group's administrator, publicly endorsed her idea and said, "I'll give you $100,000 for 10% of your profits." After that, the group followed, and Karen quickly received commitments for a half-million dollars—more

8. *See* Mary Bob's Bar, FACEBOOK, https://www.facebook.com/pages/Mary-Bobs/200744223360135 [https://perma.cc/7FZR-9LKZ] (last visited Aug. 15, 2020) (showing the Facebook page for Mary Bob's bar).

9. *See* Sissy's Cafe, FACEBOOK, https://www.facebook.com/Sissys-Cafe-185098158308681/ [https://perma.cc/349U-9RQ5] (last visited Aug. 15, 2020) (showing the Facebook page for Sissy's Café).

10. *See Beacom School of Business*, UNIV. OF S.D., https://www.usd.edu/business [https://perma.cc/JL9N-QKRA] (last visited Aug. 15, 2020) (displaying the main page of the business schools webpage highlighting themselves as a leader in the region for business education).

11. *See* NATURE'S WAY JUICE BAR, https://natureswayjuicebar.weebly.com/ [https://perma.cc/R5Q5-DSB6] (last visited Aug. 15, 2020) (displaying the webpage for Nature's Way which sells smoothies made from all natural fruits and veggies).

12. *See* Juicing for Life—Juicing Support Group, FACEBOOK, https://www.facebook.com/groups/jacquegotthejuice/ [https://perma.cc/65MR-QN3X] (last visited Oct. 25, 2020) (showing a private page for supporting those involved with juicing).

than enough to start her business.

Karen was delighted by this success but also a bit nervous because her MBA did not train her in regard to collecting funds from investors. She went to her local law firm and spoke to an attorney about her issue. He informed her that she had violated the Securities Act of 1933 by "generally soliciting" funds for her startup. Therefore, it would be illegal for her to raise money for her new business. Karen was despondent, and she left with nothing except a $550 legal bill.

B. The Big-City Businessperson

Kevin always knew he possessed the "entrepreneurial spirit." Kevin spent his adolescent summers with his family on Martha's Vineyard, where he drove a dune buggy—a gift from his parents—along the beach, selling ice cold water and soda from the buggy's cooler. When he entered Scarsdale High School—in Westchester County, New York, where families have a median household income of over $250,000—he was thrilled to learn the school had a LaunchX[13] program for high school entrepreneurs. He participated in the program and combined it with his love of golf to design a sensor that could fit in the head of the club and analyze a golfer's swing.

Kevin didn't know how to build such a sensor, but his friend Ryan was in the Robotics Club at Scarsdale High and had some ideas. After graduating high school, Kevin and Ryan matriculated to the nearby Columbia University[14] and stayed friends. Kevin studied business and Ryan studied engineering. When they graduated, they resolved to make this golf sensor idea a reality.

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13. LaunchX is a competitive four-week intensive program that provides high school students with the opportunity to start their own businesses. Admitted students receive advice from industry experts, gain exposure to potential partners and customers, and learn practical skills to tackle real business challenges, build products, and design effective business strategies. The program costs $5,450. *About the Program*, LAUNCHX, https://launchx.com/summer-program/ [https://perma.cc/S29V-GWFR] (last visited Aug. 15, 2020).

14. Columbia University and the University of South Dakota are very different institutions that afford their students different opportunities. Columbia is ranked third in the nation, whereas the University of South Dakota is tied for 263rd place. More relevantly for our two entrepreneurs, the average starting salary of a Columbia graduate is $67,500, whereas the average starting salary of a graduate from University of South Dakota is $44,000. The makeup of the student body is starkly different, too. Columbia University's student population nearly has gender parity, with 51% male students and 49% female students. The gender distribution at the University of South Dakota is 37% male students to 63% female students. *Compare Colum. U. vs. U. of S.D.*, U.S. NEWS & WORLD REP., https://www.usnews.com/best-colleges/compare?xwalk_id=190150&xwalk_id=219471 [https://perma.cc/J4RL-3DHP] (last visited Aug. 15, 2020). This has an impact on networking, especially for entrepreneurs who need venture capital, as some 93% of venture capital investors are male. Gené Teare & Ned Desmond, *The First Comprehensive Study on Women in Venture Capital and their Impact on Female Founders*, TECHCRUNCH.COM (Apr. 19, 2016 8:00 AM), https://techcrunch.com/2016/04/19/the-first-comprehensive-study-on-women-in-venture-capital/ [https://perma.cc/SX6N-E9X5].

Fortunately, Ryan's father was a lawyer, so he drafted the incorporation paperwork and paid the filing fees for the budding entrepreneurs. He also invested $10,000 as "seed money" to the newly formed GolfTec, Inc., which is acceptable under current securities regulations.[15] The team used the money to create attractive marketing materials and a rough prototype. They entered their prototype in the Columbia Entrepreneurship Innovation and Design Fast Competition and won second place. Although they did not receive any prize money, Kevin and Ryan met several investors who attended the competition and expressed interest in funding their venture. One gave Kevin his card and said, "Follow me on AngelList."

Kevin had never heard of AngelList before,[16] but he learned that it is an exclusive[17] social media network that is open only to high-wealth "accredited" investors. Companies seeking funding from these investors can also post there. Kevin recognized dozens of people he knew from Martha's Vineyard and Columbia University on the site. Kevin created a page for GolfTec, Inc., and the investor followed him. The investor's other followers followed suit, and within a week the page had over a thousand views. Using AngelList's model format for soliciting funds from accredited investors, Kevin launched a Series A financing round.[18] He took the train to Manhattan a few times to have coffee and avocado toast with some potential investors who liked the prototype that he showed them.

Within a month, GolfTec received commitments for $10 million in investments. The company hired a large New York City law firm to negotiate and paper the deal. The team paid their $30,000 legal bill from the sale proceeds and used the rest to hire two engineers and begin research and development of the GolfTec SmartCoach 1.0.

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15. This transaction would probably qualify for the private placement exemption to the registration requirement of the 1933 Securities Act under either Regulation D Rule 504 or 506. Securities Act of 1933, ch. 38, 48 Stat. 74 (codified as amended at 15 U.S.C. §§ 77a-77aa).

16. AngelList advertises itself as the "world's largest startup community." The website's offerings include employment, investment, advertisement, and research opportunities. *Join the World's Largest Startup Community*, ANGELLIST, https://angel.co/ [https://perma.cc/7ZX4-8JAV] (last visited Aug. 15, 2020).

17. *See infra* Section III.A.

18. Series A financing is typically the stage when venture capitalists—fund managers who invest other people's money—invest in start-ups. *See* Seth C. Oranburg, *The Law & Economics of the Series A Gap*, COLUMBIA L. SCH.: THE CLS BLUE SKY BLOG (Apr. 6, 2015), https://clsbluesky.law.columbia.edu/2015/04/06/the-law-economics-of-the-series-a-gap/ [https://perma.cc/F7AH-XNBG] (explaining the differences between the discrete stages of fundraising, called "series").

C. Analysis of the Problem

These hypotheticals illustrate critical points about how the general solicitation ban has a disparate impact against rural entrepreneurs. For similar reasons, the ban imposes an unfair disadvantage on anyone who is less well connected. Essentially, the ban on using social media to solicit fundraising hurts anyone who is not privileged with personal connections to wealthy investors.

Universities might play some role in leveling the playing field, but they can also tilt it further. For example, Karen's MBA program at the University of South Dakota granted her access to the Beacom Invent-to-Innovate Competition, but the first place prize in that competition is only $2,000.[19] Columbia University, on the other hand, gives out $2,400,000 to startups across campus each year.[20] While it is nominally true that both schools have business competitions, it is not reasonable to consider them equivalent where one pays out 1,200 times more money than the other.

Location also plays a huge rule in opportunity. Setting aside the prize money, consider who might attend a pitch competition in Vermillion, South Dakota, versus in New York City, New York. The CrunchBase database of startups and investors does not include any investors in Vermillion, South Dakota.[21] In addition, there is only one company headquartered there other than the University of South Dakota.[22] According to the database, there are twenty-five relevant investors in all of South Dakota.[23] In New York City, on the other hand, there are over

19. Hanna DeLange, *Beacom's Invent-to-Innovate Competition Hosted at USD*, UNIV. S.D. (Apr. 6, 2017), https://usd.edu/news/2017/beacoms-invent-to-innovate-competition-hosted-at-usd [https://perma.cc/7QJV-X92V].

20. Columbia Entrepreneurship, *Colum. Venture Competition*, COLUM. UNIV. (Apr. 6, 2018), https://entrepreneurship.columbia.edu/2018/04/06/winners-2018-columbia-venture-competition/ [https://perma.cc/7C2X-JBL6].

21. *Search Investors in Vermillion, South Dakota*, CRUNCHBASE, https://www.crunchbase.com/discover/principal.investors [https://perma.cc/XL88-W68P] (filter to investors located in Vermillion, South Dakota, to see that there are no results) (last visited Aug. 15, 2020). CrunchBase is a self-described "platform for professionals to discover innovative companies, connect with the people behind them, and pursue new opportunities. Over 55 million professionals—including entrepreneurs, investors, market researchers, and salespeople—trust Crunchbase to inform their business decisions." *About Us*, CRUNCHBASE, https://about.crunchbase.com/about-us/ [https://perma.cc/QB44-GVSS] (last visited Aug. 15, 2020).

22. *Search Companies in Vermillion, South Dakota*, CRUNCHBASE, https://www.crunchbase.com/discover/organization.companies/2fcabf2f6f86e3b2bc4e643f7ded7134 (filter to companies headquartered in Vermillion, South Dakota to see that there are only two results) [https://perma.cc/9JH4-6FHU] (last visited Aug. 15, 2020).

23. *Search Investors in South Dakota*, CRUNCHBASE, https://www.crunchbase.com/discover/principal.investors [https://perma.cc/D4HS-U7Y4] (filter to investors located in South Dakota to see that there are thirty-six results) (last visited Aug. 15, 2020).

8,000 investors[24] and over 25,000 corporate headquarters.[25] These regions are incomparable when it comes to an entrepreneur's ability to make face-to-face contact with potential investors.

The internet could provide Karen with some of the access to investors that Kevin enjoys. Scholars have recognized that social media had democratized political speech.[26] Texting, emailing, and other digital communication has supplanted or replaced analog communication forms such as phone calls and in-person conversation.[27] In particular, studies have shown that social media can enhance innovation and entrepreneurship in diverse areas such as Ontario, Canada,[28] and Nairobi, Kenya.[29]

Given the incredible power of social media to democratize society, especially with regard to creating entrepreneurship and innovation opportunities for the rural poor, why does federal law restrict its use? To answer this question thoroughly, we must go back to the beginning of the federal securities regulations and trace the thread of the general solicitation ban from its legislative intent to its modern-day application.

II. SECURITIES REGULATIONS OF GENERAL SOLICITATION

To understand the permissibility of general solicitation in securities transactions under present law, it is helpful to understand the history of the original ban on general solicitation and subsequent exemptions thereto. This part will explain the origins and developments of the general solicitation ban from its inception to present.

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24. *Search Investors in New York, New York*, CRUNCHBASE, https://www.crunchbase.com/discover/principal.investors [https://perma.cc/9YHX-76HA] (filter to investors located in New York, New York) (last visited Oct. 26, 2020).

25. *Search Companies in New York, New York*, CRUNCHBASE, https://www.crunchbase.com/discover/organization.companies/53ad1921a85c926eaf535410c6bc070e [https://perma.cc/2568-6CNL] (filter to companies headquartered in New York, New York) (last visited Oct. 26, 2020).

26. *See, e.g.*, Clay Shirky, *The Political Power of Social Media: Technology, the Public Sphere and Political Change*, 90 FOREIGN AFF. 28, 34 (2011) ("[T]he Internet spreads not just media consumption, but media production as well—it allows people to privately and publicly articulate and debate a welter of conflicting views."); CASS R. SUNSTEIN, #REPUBLIC: DIVIDED DEMOCRACY IN THE AGE OF SOCIAL MEDIA 206 (2017) (discussing the importance of free speech for political movements).

27. Agnieszka McPeak, *Disappearing Data*, 2018 WIS. L. REV. 17, 69 (2018).

28. Ataharul Chowdhury & Helen Hambly Odame, *Social Media for Enhancing Innovation in Agri-Food and Rural Development: Current Dynamics in Ontario, Canada*, 8 J. RURAL & CMTY. DEV. 97, 98 (2013).

29. Ambrose Jagongo & Catherine Kinyua, *The Social Media and Entrepreneurship Growth*, 3 INT'L J. HUMAN. & SOC. SCI. 213, 2–23 (2013).

A. Historical Background

The origins of present securities regulations can be traced back to October 24, 1929. On this day known as "Black Thursday," the Dow Jones Industrial Average (DJIA)—a market indicator consisting of a weighted average of the thirty largest publicly traded companies—lost 11% of its value.[30] Panic and chaos erupted on the trading floor. There was a brief rally on Friday as a consortium of investment bankers led by Richard Whitney purchased large blocks of shares at above-market prices.[31] But this only halted the slide before the weekend. When the markets reopened on October 28, many investors who were trading on margin determined to sell their shares, and the DJIA closed on "Black Monday" at a record loss of 13%.[32] The next day, the panic reached its zenith, and the DJIA fell an additional 12% on "Black Tuesday."[33] The market had lost over $30 billion in just two days.[34]

The Wall Street Crash of 1929 played a major role in ushering in the worldwide Great Depression that would last for years.[35] The magnitude of this financial disaster was unprecedented. All in all, the DJIA fell from a high of 5,714.08 in August 1929 to a low of 818.76 in 1932.[36] Indeed,

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30. *See A Brief History of the 1929 Stock Market Crash*, BUS. INSIDER (Apr. 8, 2018, 12:05 PM), https://www.businessinsider.com/the-stock-market-crash-of-1929-what-you-need-to-know-2018-4 [https://perma.cc/2LX2-4CGR] ("At the closing bell [on Black Thursday], the Dow Jones had fallen 11% and nearly 13 million shares had exchanged hands, triple the normal trading volume."); *Dow Jones – DJIA – 100 Year Historical Chart*, MACROTRENDS, https://www.macrotrends.net/1319/dow-jones-100-year-historical-chart [https://perma.cc/8M2T-YAY5] (last visited Aug. 15, 2020).

31. *See A Brief History of the 1929 Stock Market Crash*, *supra* note 30 ("To stem the rising panic, Richard Whitney, president of the New York Stock Exchange and lead broker for J.P. Morgan bid $10 higher than the previous per-share bid for 25,000 shares of U.S. Steel. The strategy worked and the market rebounded.")

32. *See* Claire Suddath, *Brief History of the Crash of 1929*, TIME (Oct. 29, 2008), http://content.time.com/time/nation/article/0,8599,1854569,00.html [https://perma.cc/Q286-LUEN] ("By the end of the day, the Dow had dropped 13%. So many shares changed hands that day that traders didn't have time to record them all."); *Stock Market Crash of 1929*, BRITANNICA ACADEMIC, https://www.britannica.com/event/stock-market-crash-of-1929 [https://perma.cc/498G-P5VQ] ("The panic began again on Black Monday (October 28), with the market closing down 12.8 percent.") (last visited Aug. 20, 2020).

33. *See Stock Market Crash of 1929*, ENCY. BRITANNICA, https://www.britannica.com/event/stock-market-crash-of-1929 [https://perma.cc/8UYD-KFS4] (last visited Aug. 15, 2020) ("On Black Tuesday (October 29) more than 16 million shares were traded. The Dow lost another 12 percent and closed at 198—a drop of 183 points in less than two months.").

34. *See* Clay Halton, *Black Tuesday*, INVESTOPEDIA (MAY 1, 2020), https://www.investopedia.com/terms/b/blacktuesday.asp [https://perma.cc/CR48-GJSK] (discussing the stock market crash of 1929); *see also* Suddath, *supra* note 32 ("In total, $25 billion—some $319 billion in today's dollars—was lost in the 1929 crash.").

35. *See* Christina D. Romer & Richard H. Pells, *Great Depression*, ENCYC. BRITANNICA (Sept. 10, 2020), https://www.britannica.com/event/Great-Depression [https://perma.cc/C7VW-3JA8].

36. *Dow Jones - DJIA - 100 Year Historical Chart*, *supra* note 30 (adjusting for inflation).

it would not be until May 1959 that the market would fully recover from this loss, when the market finally hit 5,770.29.[37]

The impact of the crash was not merely economic but political and legal as well. American citizens were unemployed and angry. The psychological effects of the crash are well documented elsewhere, and it is beyond the scope of this Article to explain them or to argue which causes resulted in which effects. But a sweeping change in American politics is obvious even to the casual observer. Incumbent President Herbert Hoover, who presided during the Crash, lost the 1932 presidential election in a landslide victory for Franklin Delano Roosevelt (FDR).[38] FDR, for his part, won that 1932 election after a campaign promising traditional economic policies including a balanced budget.[39] But by FDR's 1936 reelection campaign, he had completely changed his tune and adopted (his version of) Keynesian economic theory and Brandeisian regulatory theory.

Keynesian economics—the brainchild of John Maynard Keynes, who published *The General Theory of Employment, Interest, and Money* in 1936—essentially posits that, in the short run, governments can lessen the severity of recessions and depressions by spending.[40] In simplified Keynesian terms, recessions are periods when aggregate demand is low. Government investment in infrastructure and similar government expenditures can increase demand by injecting cash directly into the economy, which can create jobs and increase output, sometimes with a multiplier factor.[41] This stimulation can lessen, or even reverse, the harsh effects of unemployment and decreased demand during a period of economic downturn.[42] Keynes also advocated for the Federal Reserve to

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37. *Id.*

38. *See United States Presidential Election of 1932*, ENCYC. BRITANNICA, https://www.britannica.com/event/United-States-presidential-election-of-1932 [https://perma.cc/SJ9L-V9V8] (last visited Aug. 30, 2020) (providing a historical overview of the 1932 election).

39. *See id.* ("In a series of addresses carefully prepared by a team of advisers popularly known as the Brain Trust, [Roosevelt] promised aid to farmers, public development of electric power, a balanced budget, and government policing of irresponsible private economic power.").

40. *See generally* JOHN MAYNARD KEYNES, THE GENERAL THEORY OF EMPLOYMENT, INTEREST, AND MONEY (General Press 2019) (detailing what is Keynesian economics and how spending can help).

41. Alan S. Blinder, *Keynesian Economics*, LIBR. ECON. & LIBERTY, https://www.econlib.org/library/Enc/KeynesianEconomics.html [https://perma.cc/QFW7-C9ZV] (last visited Aug. 15, 2020) (explaining that Keynesian economic theory promotes a lowering of interest rates during the "bust" cycle to promote private borrowing).

42. *See generally* Sarwat Jahan et al., *What Is Keynesian Economics?*, 51 FIN. & DEV. (IMF Sept. 2014), https://www.imf.org/external/pubs/ft/fandd/2014/09/basics.htm [https://perma.cc/HE98-NRLF] (discussing the basic tenets of Keynesian economics).

reduce interest rates to promote private borrowing and spending[43] and to discourage excessive saving.[44] It is critical to note that Keynesian economics puts the federal government in a much more active role vis-à-vis the economy as compared with classical economic theory (which generally proscribed a laissez-faire role of government).[45]

Keynes met FDR on May 28, 1934 and explained his theories to the president in considerable detail.[46] After their meeting, Keynes met with Secretary of Labor Frances Perkins and clarified the multiplier effect in oversimplified terms. He explained that a dollar spent by the government on a public work's project is a dollar given to the grocer, who in turn spends that dollar on supplies from the wholesaler, who in turn spends that dollar on supplies from the farmer, essentially creating four dollars' worth of output from a one dollar investment.[47] Perkins later noted that Keynes may have overestimated FDR's understanding of the underlying mathematical principles behind his ideas and that the meeting may have been more productive if Keynes had explained his theories in layman's terms, as he had done with Perkins.[48]

Although their initial meeting was brief, Keynes made a profound impact on the president, who was then a vocal opponent of the classical laissez-fair role of the government. Inspired by Keynes's theories, FDR's New Deal set about an unprecedented expansion of the federal government that FDR enacted between 1933 and 1938.[49] It included the

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43. *What is Keynesian Economic Theory?* CORP. FIN. INST., https://corporatefinanceinstitute.com/resources/knowledge/economics/keynesian-economic-theory/ [https://perma.cc/VL8A-9QA5] (last visited Aug. 15, 2020).

44. Jim Chappelow, *Keynesian Economics*, INVESTOPEDIA, (updated Apr. 30, 2020) https://www.investopedia.com/terms/k/keynesianeconomics.asp [https://perma.cc/5S2J-FJ4J] ("Keynes also criticized the idea of excessive saving, unless it was for a specific purpose such as retirement or education. He saw it as dangerous for the economy because the more money sitting stagnant, the less money in the economy stimulating growth. This was another of Keynes's theories geared toward preventing deep economic depressions.").

45. *Compare Keynesian Economics*, ENCYC. BRITANNICA https://www.britannica.com/topic/Keynesian-economics [https://perma.cc/6D9C-97NG] (Apr. 18, 2017), *with Laissez-faire Economics*, ENCYC. BRITANNICA, https://www.britannica.com/topic/laissez-faire [https://perma.cc/XM4N-BPQ9] (Oct. 29, 2019).

46. *See May 28th, 1934*, FRANKLIN D. ROOSEVELT: DAY BY DAY, PARE LORENTZ LIB., http://www.fdrlibrary.marist.edu/daybyday/daylog/may-28th-1934/ [https://perma.cc/XWU6-3HEK] (last visited Aug. 15, 2020) (providing a log of the president's activities for May 28, 1934).

47. NICHOLAS WAPSHOTT, KEYNES HAYEK: THE CLASH THAT DEFINED MODERN ECONOMICS 161–62 (2011).

48. *See* FRANCES PERKINS, THE ROOSEVELT I KNEW 9 (1946) (recalling that, after Keynes's meeting with FDR, Keynes mentioned to then-Secretary of Labor, Frances Perkins, that "he had 'supposed the President was more literate, economically speaking.'").

49. *See generally New Deal: United States History*, ENCYC. BRITANNICA (Dec. 3, 2019), https://www.britannica.com/event/New-Deal [https://perma.cc/MA9W-YA6A] (FDR's New Deal brought economic relief and reforms to agriculture, finance, waterpower, labor, and housing, industries greatly increasing he scope of the federal government's scope).

creating of the Civilian Conservation Corps,[50] the Public Works Administration, the Works Progress Administration, the Resettlement Administration, the Rural Electrification Administration, the Civil Works Administration, the Farm Security Administration, the Federal Crop Insurance Corporation, the Social Security Administration, and other government agencies and programs.[51]

These programs were obviously not free. Coincidentally, with the expansion of the federal government came a great increase in income taxes. In 1931, the highest tax rate was 25%, and the average taxpayer paid $76.30 in federal income taxes.[52] The IRS collected a total of $246 million in income tax that year.[53] By 1940, the highest rate was 79%,[54] and the IRS collected $6.548 billion.[55]

On the regulatory front, FDR was inspired by another leading thinker of the day, Justice Louis Dembitz Brandeis. Brandeis was an American Jew born to immigrant parents from Bohemia who raised him in a secular home. Despite these humble beginnings, Brandeis graduated Harvard Law School at age twenty and founded a law firm in Boston. Perhaps because of his background, Brandeis became well recognized as the "People's Lawyer" through his leadership for progressive social causes.[56]

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50. The Civilian Conservation Corps created many of America's national parks. *The Civilian Conservation Corporations Timeline: The Evolution of the CCC*, PBS, https://web.archive.org/web/20161225041953/https://www.pbs.org/wgbh/americanexperience/features/timeline/ccc/ (noting that FDR signed the Federal Unemployment Relief Act into law on March 31, 1933, and this law created the program commonly known as the Civilian Conservation Corps, or "CCC"); *Civilian Conservation Corps*, HISTORY (Oct. 17, 2018), https://www.history.com/topics/great-depression/civilian-conservation-corps [https://perma.cc/GLR9-LWDA] (describing the CCC as a work relief program that put millions of young men to work, creating the national and state park systems that we enjoy today).

51. *See also New Deal Programs*, LIVING NEW DEAL, (May 20, 2020) https://livingnewdeal.org/what-was-the-new-deal/programs/ [https://perma.cc/3QZX-9E46] (last visited August 27, 2020) (listing all the programs and agencies created by the New Deal).

52. STATISTICS OF INCOME FOR 1931, U.S TREASURY DEPARTMENT BUREAU OF INTERNAL REVENUE 4, 8 (1933), https://www.irs.gov/pub/irs-soi/31soirepar.pdf [https://perma.cc/DB2G-25HG] ("The average net income for 1931 was $4,217.40 for all returns and $6,094.22 for taxable returns, the average amount of tax liability was $76.30 for all returns and $161.34 for taxable returns, and the average tax rate was 1.81 percent for all returns and 2.65 percent for taxable returns.").

53. *Id.* at 6 (showing simple and cumulative distribution of individual returns for 1931, by net income classes, number of returns, net income, tax, and percentages).

54. *U.S. Federal Individual Income Tax Rates History, 1862–2013*, TAX FOUND. (Oct. 17, 2013), https://taxfoundation.org/us-federal-individual-income-tax-rates-history-1913-2013-nominal-and-inflation-adjusted-brackets/ [https://perma.cc/DTH5-9LVA].

55. *Federal Tax Revenue by Source, 1934–2018*, TAX FOUND. (Nov. 21, 2013), https://taxfoundation.org/federal-tax-revenue-source-1934-2018/ [https://perma.cc/QE6C-ASNY] (chart revealing Federal Government receipts by source in millions of dollars).

56. *See Louis Brandeis*, ENCYC. BRITANNICA (Nov. 9, 2019), https://www.britannica.com/biography/Louis-Brandeis [https://perma.cc/GN98-2F3R] (discussing Brandeis' characteristics that led to him being called the "People's Lawyer").

Brandeis was notably anti-corporate. He denounced "cutthroat competition" and, ironically, also denounced the evils of monopoly:

> We learned long ago that liberty could be preserved only by limiting in some way the freedom of action of individuals; that otherwise liberty would necessarily yield to absolutism; and in the same way we have learned that unless there is regulation of competition, [capitalism's] excesses will lead to the destruction of competition, and monopoly will take its place.[57]

In 1914, Brandeis published the book *Other People's Money and How the Bankers Use It*, which attacked investment funds and called for a breakup of the so-called Money Trust.[58] He also coined a phrase which would become the watchwords of the New Deal regulatory regime: "Publicity is justly commended as a remedy for social and industrial diseases. Sunlight is said to be the best of disinfectants; electric light the most efficient policeman."[59]

In 1916, President Woodrow Wilson nominated Brandeis to the Supreme Court, to which he was confirmed on June 1 of that year.[60] During his subsequent twenty-three years of service on the bench, Brandeis became one of the most influential members of that high court. Jacket Library Publishers reprinted Brandeis's polemic essays in 1933,[61] resurrecting the attack on investment funds reflected in popular opinion at the time. American sentiment favored expansive New Deal regulations. *Other People's Money* supported the breakup of the Money Trust. Its more famous passages are often quoted in support of New Deal-era securities regulations.[62]

And those New Deal regulations were numerous. During FDR's term,

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57. Louis B. Brandeis, The Regulation of Competition Versus the Regulation of Monopoly, Address to the Economic Club of New York (Nov. 1, 1912) (transcript available at Louis D. Brandeis School of Law Library), https://louisville.edu/law/library/special-collections/the-louis-d.-brandeis-collection/the-regulation-of-competition-versus-the-regulation-of-monopoly-by-louis-d.-brandeis [https://perma.cc/7H5M-86FE].

58. LOUIS BRANDEIS, OTHER PEOPLE'S MONEY AND HOW THE BANKERS USE IT 69–91 (1914) (explaining the Serve One Master Only advice on regulating the Money Trust); *id.* at 4–6 (The Money Trust was the concept that investment bankers had abused the public trust and taken control of numerous industries.).

59. BRANDEIS, *supra* note 58 at 92 (discussing the role publicity played in the struggle against the Money Trust).

60. *See* Andrew Glass, *Wilson Nominates Brandeis to Supreme Court, Jan. 28, 1916*, POLITICO (Jan. 28, 2019 12:00 AM), https://www.politico.com/story/2019/01/28/this-day-in-politics-january-28-1124759 [https://perma.cc/N2XS-E7AC] (providing that on June 1, 1916, the Senate confirmed Brandeis to the Supreme Court by a 47-22 vote).

61. LOUIS BRANDEIS, OTHER PEOPLE'S MONEY AND HOW THE BANKERS USE IT (Jacket Libr. Publishers 1933) (1914).

62. BRANDEIS, *supra* note 58, at 92 (Perhaps the most famous line in *Other People's Money* is its ringing endorsement of public disclosure regimes: "Sunlight is said to be the best of disinfectants; electric light the most efficient policeman.").

and very much owing to Roosevelt's influence, Congress passed the Emergency Banking Relief Act, the Economy Act, the Beer-Wine Revenue Act, the Federal Emergency Relief Act, the Agricultural Adjustment Act, the Tennessee Valley Authority Act, the National Employment System Act, the Securities Act, the Home Owners Loan Act, the National Industrial Recovery Act, the Glass-Steagall Act, the Gold Reserve Act, the Securities Exchange Act, the Indian Reorganization Act, the National Housing Act, the Federal Farm Bankruptcy Act, the Emergency Relief Appropriation Act, the National Labor Relations Act, the Social Security Act, the Banking Act, the Revenue Act, the Soil Conservation Act, the Farm Tenant Act, the Housing Act, the Fair Labor Standards Act, and other regulations.[63]

The precise nature of all the foregoing regulations is not critical for present purposes of this Article, although it is critical to understand the zeitgeist of the era. The Securities Act of 1933, however, is paramount.

B. The Securities Act of 1933

The Securities Act of 1933,[64] also known as the Truth in Securities Act, was very much predicated on the Brandeisian concept of "sunlight is the best disinfectant." The Securities Act created a registration and disclosure regime with which issuers must comply before selling any securities via an instrumentality of interstate commerce.[65] Securities are defined broadly as to include stocks, investment contracts, and other equity positions.[66] Instrumentalities of interstate commerce were likewise defined broadly, such that any use of the telephone or mail in the offer or sale of stock would probably cause that transaction to come under the purview of the Securities Act.[67]

Registering an offer or sale of securities under the Securities Act requires the public disclosure of any and all information that a reasonable shareholder would find material in deciding whether to purchase the securities.[68] However, registering under the Securities Act is expensive,

63. *See* Kimberly Amadeo, *New Deal Summary, Programs, Policies, and Its Success*, THE BALANCE (July 31, 2020), https://www.thebalance.com/fdr-and-the-new-deal-programs-timeline-did-it-work-3305598#first-new-deal-and-its-programs [https://perma.cc/8PAY-3QL5] (summarizing the New Deal programs and regulations); *see New Deal Programs*, *supra* note 51 (listing the New Deal programs with brief summaries).

64. Securities Act of 1933, ch. 38, 48 Stat. 74 (codified as amended at 15 U.S.C. §§ 77a-77aa).

65. *See* Securities Act of 1933, § 5 (outlining prohibitions related to interstate commerce and mail).

66. § 2(a)(1).

67. § 5.

68. §§ 6–8.

time consuming, and uncertain, such that it is best avoided if possible.[69]

Fortunately, there are two exemptions built into the Securities Act itself. Broadly speaking, there are exempt securities and exempt transactions. Exempt securities, as described in section 3 of the Securities Act, can always be sold or resold without registration, but most startup companies do not qualify for these exemptions.[70] Section 3 is primarily used by national banks and the federal government. Rather, it is section 4—which describes exemption transactions—that would be the key exemption for the vast majority of startups and small businesses.[71]

1. Section 3(b)

When the Securities Act was originally promulgated by the Seventy-Third Congress on May 27, 1933, it exempted several specific classes of securities in section 3(a).[72] These exemptions generally do not apply to startup companies, but Congress also granted the SEC permission to exempt additional classes. Section 3(b) originally said:

> The commission may from time to time by its rules and regulations, and subject to such terms and conditions as may be prescribed therein, add any class of securities to the securities exempted as provided in this section, if it finds that the enforcement of this title with respect to such securities is not necessary in the public interest and for the protection of investors by reason of the small amount involved or the limited character of the public offering; but no issue of securities shall be exempted under this subsection where the aggregate amount at which such issue is offered to the public exceeds $100,000.[73]

Also known as the "Small Issue Exemption," section 3(b) was subsequently amended several times to increase the maximum offering amount.[74] Under the current version of the statute, the maximum offering that can qualify under section 3(b) is $5,000,000.[75]

Four aspects of this provision are noteworthy. First, this exemption

69. *See id.* (This, of course, raises the question of who is the "reasonable shareholder" envisioned by the Securities Act? It is not necessary to resolve this question for the present purposes of this Article, but it is worth mentioning that while there are quite a few very good articles on that subject, there are none that address who the reasonable shareholder in social media investing is. The author of this Article plans to address that gap in the literature in future work.).

70. *See generally* Securities Act of 1933, § 3 (detailing the exempt securities).

71. *See generally* § 5 (detailing exemption transactions).

72. Securities Act of 1933 § 3(a).

73. § 3(b).

74. *See, e.g.*, An Act to amend the Securities Investor Protection Act of 1970, Pub L. No. 95–283, §18, 92 Stat. 275 (1978) (increasing the maximum offering amount from $500,000 to $1,500,000).

75. 15 U.S.C. § 77c(b)(1) ("No issue of securities shall be exempted under [small issues exemptive authority] where the aggregate amount at which such issue is offered to the public exceeds $5,00,000.").

applies to the securities themselves, not the transaction. This means that securities issued under this provision could be resold in another transaction because the exemption attaches to the security. This resale exemption is presently of little consequence, however, because the SEC has specifically ruled that its permissive exemptions under 3(b) are subject to resale restrictions.[76] Yet it appears this resale restriction is not required by the statute.

Second, this exemption is permissive, whereby the SEC *may* create a rule or regulation.[77] This distinguishes the 3(b)(1) from the 4(a)(2) exemption described below, as the latter provides that certain transactions are exempt from the Securities Act as a matter of statutory law. Third, the Small Issue Exemption is limited to a dollar amount that is specified by Congress as a matter of statutory law. While the SEC can set a lower limit, it does not have the authority to set a higher limit for exempt securities under this section.

Fourth, the section 3(b)(1) exemption contemplates a "limited character of the public offering."[78] This is nebulous on two dimensions, as the terms "limited character" and "public offering" are both unclear. It would seem, however, that section 3(b)(1) provides room for a broader

76. *See* 17 C.F.R. § 230.502(d) (2019) ("Except as provided in § 230.504(b)(1), securities acquired in a transaction under Regulation D shall have the status of securities acquired in a transaction under section 4(a)(2) of the Act and cannot be resold without registration under the Act or an exemption therefrom."). *See also* 17 C.F.R. § 230.504(b)(1) (2019).

General conditions. To qualify for exemption under this § 230.504, offers and sales must satisfy the terms and conditions of §§ 230.501 and 230.502(a), (c) and (d), except that the provisions of § 230.502(c) and (d) will not apply to offers and sales of securities under this § 230.504 that are made:

> (i) Exclusively in one or more states that provide for the registration of the securities, and require the public filing and delivery to investors of a substantive disclosure document before sale, and are made in accordance with those state provisions;
> (ii) In one or more states that have no provision for the registration of the securities or the public filing or delivery of a disclosure document before sale, if the securities have been registered in at least one state that provides for such registration, public filing and delivery before sale, offers and sales are made in that state in accordance with such provisions, and the disclosure document is delivered before sale to all purchasers (including those in the states that have no such procedure); or
> (iii) Exclusively according to state law exemptions from registration that permit general solicitation and general advertising so long as sales are made only to "accredited investors" as defined in § 230.501(a).

77. *See* Securities Act of 1933, ch. 38, § 3(b)(1), 48 Stat. 74 (codified as amended at 15 U.S.C. §§ 77a-77aa). ("The Commission *may* from time to time by its rules and regulations, and subject to such terms and conditions as may be prescribed therein, add any class of securities to the securities exempted as provided in this section, if it finds that the enforcement of this subchapter with respect to such securities is not necessary in the public interest and for the protection of investors by reason of the small amount involved or the limited character of the public offering . . . .") (emphasis added).

78. *Id.*

reading of "public offering" than section 4(a)(2), which only pertains to transactions "not involving a public offering."[79]

This last point merits emphasis. If one is to follow the common rules of statutory construction that similar terms should be interpreted in a similar way and different terms should be interpreted in a different way,[80] then this difference in language indicates a difference in meaning. It logically follows that "limited public offering" and "not . . . a public offering" are distinguishable. Moreover, "limited" seems to indicate a broader scope of permitted activity than "not" or none. Therefore, 3(b)(1) should be interpreted to be more permissive than 4(a)(2) with regard to public offerings. Thus, the offer and sale on social media of securities exempted under section 3(b)(1) may be less likely to violate the securities laws than a similar offer and sale of securities in a transaction exempted under section 4(a)(2).

2. Section 4(a)(2)

The original version of the Securities Act provided in section 4(1) the prohibitions of the Securities Act "[s]hall not apply to . . . transactions by an issuer not with or through an underwriter and not involving any public offering."[81] Now found in section 4(a)(2), the current version of the Securities Act, as amended, provides that "[t]he provisions of section 5 [prohibitions relating to interstate commerce and the mails] shall not apply to transactions by an issuer not involving any public offering."[82] It is important to note that a "public offering" disqualifies an issuance of stock from exemption under section 4(a)(2).

This brings up yet another question: what is a "public offering"? The SEC first attempted to answer this question on January 24, 1935, when it published an opinion letter outlining four factors that would be considered in determining whether a public offering is involved in a given transaction: (1) the number of offerees and their relationship to each other and to the issuer; (2) the number of units offered; (3) the size of the offering; and (4) the manner of the offering.[83]

Unfortunately, this multifactor test did little to provide the clarity and certainty needed for unregistered offerings. Rather, it provided as many

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79. § 4(a)(2).

80. *See* William N. Eskridge, Jr. & Philip P. Frickey, *The Supreme Court 1993 Term Foreword: Law as Equilibrium*, 108 HARV. L. REV. 26, 99, 105 (1994) (provides the Rehnquist court's canons of statutory construction).

81. Securities Act of 1933, ch. 38, § 4(1), 48 Stat. 74 (codified as amended at 15 U.S.C. §§ 77a–77aa).

82. § 4(a)(2).

83. Letter of Gen. Counsel Discussing Factors to be Considered in Determining the Availability of the Exemption from Registration Provided by the Second Clause of Section 4(1), Securities Act Release No. 285, 1935 WL 27785 (Jan. 24, 1935).

new questions as it did answers. For instance, how many units can be offered before an offering becomes public? The SEC first attempted to clarify the statue by ruling that the Securities Act only applied when a "substantial number" of securities was offered to the public.[84] What, precisely, is a "substantial number"? This question does not even bear further consideration, given that in 1953, the Supreme Court expressly held that "there is no warrant for superimposing a quantity limit on private offerings as a matter of statutory interpretation."[85]

SEC v. Ralston Purina Co.[86] is a foundational case in securities law because it was the first time that the Supreme Court attempted to define a public offering. Ralston Purina, a Missouri-based manufacturer of animal feed and pet food, offered shares of its stock to a number of its "key employees."[87] The corporation made no effort to register this transaction under the Securities Act of 1933, and the key employees were not given access to the kind of information which registration under the Act. The corporation argued that offering to a limited group (such as key employees or even all employees) could not properly be characterized as a public offering.

The Supreme Court rejected this argument. It found that employees are members of the investing public and are thereby entitled to the same protections under the Securities Act.[88] The Court conceded that some employees, such as high-level executives, might have access to the same kind of information that would be required by a registration. If the offering was confined to such high-level executives, then perhaps that would not be a public offering. But this is dicta.

The critical holding from *Ralston Purina* is that an offering that is not open to everyone may nevertheless be public in character. Whether an offering is "public" and "private" requires a fact-specific inquiry into the circumstances under which the distinction is sought to be established, and to consider the purposes sought to be achieved by such distinction.[89]

84. Securities Act Release No. 97, 1933 WL 28905 at *3 (Dec. 28, 1933) ("It seems clear that offerings addressed only to security holders of a single issuer may nevertheless be 'public offerings' within the meaning of Section 4(1) . . . . If the group of security holders includes a substantial number of persons, the offering should be considered a 'public' one."); *See also* Securities Act Release No. 285, at *1 (holding that twenty-five persons was not a "substantial number").

85. SEC v. Ralston Purina Co., 346 U.S. 119, 125 (1953) (discussing when to investigate particular exemption claims).

86. *Id.* at 120.

87. *Id.* (discussing that a "key employee" is within this exemption).

88. *Id.* at 126–27 (holding that Provision of Securities Act, exempting from registration requirements transactions by an issuer not involving any public offering, was not intended to deprive employees as a class of the safeguards of the Provision of Securities Act).

89. *Id.* at 124 (citing 102 F. Supp. at 968, 969).

Ralston Purina provided two requirements for an offering to be characterized as private. First, all offerees must have access to the types of information that would be disclosed in a registration; and, second, the offerees must be capable of fending for themselves.[90] The second requirement has developed into the "sophisticated investor" standard, which includes an assessment of offerees' ability to demand and understand the information that is available to them.[91] In other words, the Court found that access to information is a necessary but not a sufficient condition to find that the investor is able to fend for oneself.[92]

The Court explained that the number of purchasers involved is not dispositive, but the number of offerees and purchases is a relevant factor in determining whether an offering is private.[93] The size of the offering is also relevant to this determination. Both the number of shares of stock offering and the aggregate offerings price of the transaction help show whether an offering is public or private.[94]

In summary, *Ralston Purina* held that whether an offering is public or private shall be based on (1) the number of offerees, (2) the offerees' need for information, (3) the offerees' access to information, and (4) the size of the offering—both in terms of the number of securities offered and the aggregate offering price.[95]

The SEC again tried to clarify the concept of "public offering" in 1974 by adopting Rule 146.[96] After its adoption, then-SEC Chairman William J. Casey proudly remarked, "[a]fter 40 years of mystery and uncertainty, we published this week standards on how companies can raise money in a private offering,"[97] and further promised to "provide more objective

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90. *Id.* at 124–25 (referencing Thomas Lee Hazen, *§ 4:88. Exemption for Issuer Transactions Not Involving a Public Offering ("The Private Placement Exemption")—Section 4(a)(2)—Scope of the Section 4(a)(2) Exemption*, 1 LAW SEC. REG. § 4:88 (2020)).

91. *Id.* (discussing how the design of the statute is to protect investors by promoting full disclosure of information necessary for investors to make informed investment decisions).

92. *Id.* at 124–127 (discussing other necessary skills and knowledge needed for investors).

93. *Ralston Purina*, 346 U.S. at 125.

94. *Id.* at 122, n. 6 (explaining the sale of stockholders that are small in numbers does not constitute a public offering).

95. Hazen, *supra* note 90 (providing factors to determine whether an offering is public or private).

96. *See* Noticed of Proposed Rule 146 Under the Securities Act of 1933 – "Transactions by an Issuer Deemed Not to Involve Any Public Offering and Related Form 146" and Notice of a Proposal to Amend Rule 257 Under Such Act – "Offerings Not in Excess of $50,000", Securities Act Release No. 5336, 1972 WL 121503 (Nov. 28, 1972) (providing more objective standards for determining a public offering).

97. SEC News Release, Remarks by William J. Casey, Chairman, SEC, Regulation and the Structure of the Securities Market (Nov. 30, 1972); Gregory DuBois Erwin, *Goodbye Private Placement, Hello 146 – Recent Appellate Court Decisions Suggest that Investment Bankers Should No Longer Rely on the Private Placement Exemption*, 6 CREIGHTON L. REV. 127, 127 (1972) (emphasizing the uncertainty as to what constitutes a private offering).

standards for determining when the offer or sale of securities by an issuer is a transaction not involving a public offering."[98]

While Rule 146 was clear and quantitative insofar as limiting the number of purchasers to thirty-five, it suffered from numerous ambiguities pertaining to general solicitation. For example, Rule 146 provided that the offer must be made to an investment representative that "has such knowledge and experience in financial and business matters that he alone, or together with other offeree representatives or the offeree, is capable of evaluating the merits and risks of the proposed investment."[99] This effectively restates the "sophisticated investor" requirement without clarifying what that means. Others have noted that "this is a very imprecise standard, and courts have, predictably, differed in their interpretations of it."[100] As it turned out, Rule 146 was so vague as to be essentially useless, and it has been relegated to the voluminous dustbin of securities law history.

The SEC tried yet again—and perhaps finally succeeded—in 1982 with its adoption of Regulation D.[101] Affectionately called "Reg D," this regulation created reasonably clear ways for offerings to be exempt from registration under the Securities Act.[102] Indeed, this regulation paved the way for the venture capital industry to succeed in America.

C. Regulation D

When Regulation D was promulgated on April 15, 1982, it comprised six rules, Rules 501–506.[103] The first three rules set forth general terms and conditions: Rule 501 defines "accredited investor," "insiders," "natural persons," "purchaser representative," and other key terms; Rule 502 sets forth the disclosure requirements (which are minimal) and

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98. Transactions By an Issuer Deemed not to Involve Any Public Offering, Securities Act Release No. 5487, 39 Fed. Reg. 15,261 (May 2, 1974) (discussing objective standard to determine what would not be deemed a public offering).

99. Securities Act Release No. 5487, 39 Fed. Reg. at 15,263 (SEC Rule 146(a)(1)(i)) (discussing the knowledge and expertise needed to be capable of evaluating proposed investments).

100. H. David Heumann, *Is SEC Rule 146 Too Subjective to Provide the Needed Predictability in Private Offerings?*, 55 NEB. L. REV. 1, 7 (1975) (discussing the imprecise standard of investment sophistication).

101. *See* 17 C.F.R. § 230.501 *et seq.* (2019) (explaining the sections and terms used in Regulation D).

102. *Id. See also Regulation D Offerings*, SEC, https://www.sec.gov/fast-answers/answers-regdhtm.html [https://perma.cc/U5VV-GMEF] (Nov. 27, 2017) (explaining how companies can become exempt from registration requirements under Regulation D).

103. *See* Revision of Certain Exemptions from Transactions Involving Limited Offers and Sales, Securities Act Release No. 6389, 24 SEC. Docket 1166, 1982 WL 35662, at *2 (Mar. 8, 1982) ("Rules 501-506, that establishes three exemptions from the registration requirements of the Securities Act and replaces exemptions that currently exist under Rules 146, 240, and 242."); Interpretive Release on Regulation D, Securities Act Release No. 6455, 1983 WL 409415 (Mar. 3, 1983).

establishes other terms of the offering; and Rule 503 requires the issuer to file a notice of sale on Form D.[104] Additionally, Rule 502(c) prohibits the issuer from any form of general solicitation or general advertising.[105] The SEC provided an interpretive release on Regulation D that attempts to define "general solicitation":

> In analyzing what constitutes a general solicitation, the staff considered a solicitation by the general partner of a limited partnership to limited partners in other active programs sponsored by the same general partner. In determining that this did not constitute a general solicitation, the Division underscored the existence and substance of the preexisting business relationship between the general partner and those being solicited. The general partner represented that it believed each of the solicitees had such knowledge and experience in financial and business matters that he or she was capable of evaluating the merits and risks of the prospective investment . . . .
>
> In analyzing whether an issuer was using a general advertisement to offer or sell securities, the staff declined to express an opinion on a proposed tombstone advertisement that would announce the completion of an offering . . . . Because the requesting letter did not describe the proposed use of the tombstone announcement, and because the announcement of the completion of one offering could be an indirect solicitation for a new offering, the staff did not express a view. In a letter regarding Tax Investment Information Corporation dated January 7, 1983, the staff considered whether the publication of a circular analyzing private placement offerings, where the publisher was independent from the issuers and the offerings being analyzed, would violate Rule 502(c). Although Regulation D does not directly prohibit such a third-party publication, the staff refused to agree that such a publication would be permitted under Regulation D because of its susceptibility to use by participants in an offering. Finally, in the letter re Aspen Grove dated November 8, 1982 the staff expressed the view that the proposed distribution of a promotional brochure to the members of the "Thoroughbred Owners and Breeders Association" and at an annual sale for horse owners and the proposed use of a magazine advertisement for an offering of interests in a limited partnership would not comply with Rule 502(c).[106]

As the above discussion makes clear, the ban on general solicitation was murky and contested right from its start. It is even harder to relate the SEC's guidance on general solicitation to the use of social media

104. *See* Securities Act Release No. 6455, 1938 WL 409415, at *1 (Mar. 3, 1938) ("[Rules 501-503] set forth general terms and conditions that apply in whole or in part to the exemptions.").

105. *Id.* ("Rule 502(c) prohibits the issuer or any person acting on the issuer's behalf from offering or selling securities by any form of general solicitation or general advertising.").

106. Interpretive Release on Regulation D, Securities Act Release No. 6455, 1983 WL 409415 (Mar. 3, 1983) (internal citations omitted) (quoting "Manner of Offering – Rule 502(c)").

today. While the ban on general solicitation has been lifted with regard to offerings made solely to accredited investors, it remains in effect for offerings to ordinary investors. Such offerings can be vital to early stage startups who raise most of their seed money from friends and family.[107] Accordingly, the exemptions that permit sale to ordinary investors—Rule 504 and Rule 506(b)—remain highly relevant and require further analysis. Both of these exemptions are conditional on meeting the requirement of Rule 502(c), which limits the manner of offering and bans general solicitation.[108]

1. Rule 502(c)

Rule 502(c) bans general solicitation and defines it as "including, but not limited to, the following: (1) Any advertisement, article, notice or other communication published in any newspaper, magazine, or similar media or broadcast over television or radio; and (2) Any seminar or meeting whose attendees have been invited by any general solicitation or general advertising."[109]

The ban on general solicitation focuses on the quality, rather than the quantity, of potential investors. In other words, general solicitation may be prohibited even if relatively few potential investors are contacted if the investors lack sophistication, wealth, or experience in the industry. On the other hand, general solicitation of a relatively large group of potential investors may not be prohibited if those investors meet the qualification requirements for that offering. In order to constitute a general solicitation, promoters and issuers of the offering must not have a prior relationship with the offeree. Underwriters are often used to ensure that the offerees meet the necessary requirements or have made prior deals with issuers. Mass mailings, along with targeted mailings through the purchase of mailing lists, are typical examples of general solicitations. Further, the construction of any mailing list will constitute general solicitation unless the potential investors on the mailing list have been properly vetted prior to its formulation.[110]

It is clear that use of electronic media can constitute a general solicitation but limiting access to such media can comply with the no-

107. *See Types of Investors*, FUNDABLE, https://www.fundable.com/learn/resources/guides/investor/types-of-investors [https://perma.cc/24VK-2CPH] (last visited May 24, 2020) (calculating $60 billion of funding for startups comes from family and friends in the aggregate each year in the United States whereas $20 billion comes from angel investors, $22 billion from venture capitalists, and $2.8 billion from actual customers).

108. *See* 17 C.F.R. § 230.502(c) (2020) (noting the limitations on the manner of an offering).

109. *Id.* (providing the definition for general solicitation).

110. Thomas Lee Hazen, *§ 4:77. Regulation D—Limitations on General Solicitation in Regulation D Offerings*, 1 LAW SEC. REG. § 4:77 (2020) (explaining how the construction of a mailing list constitute general solicitation).

general-solicitation provision on Rule 502(c). For example, in the early days of the internet, the SEC stated that "the placing of the offering materials on the Internet would not be consistent with the prohibition against general solicitation or advertising in Rule 502(c) of Regulation D."[111] However, the SEC has since taken a more nuanced view toward internet materials. In 1996, the SEC issued a no-action letter regarding IPOnet, approving the use of a password-protected website for private placements, provided that investors could only access the information after they had been qualified as "sophisticated."[112] Subsequent SEC guidance confirmed its position that providing investment information on a password-protected web site does not amount to a general solicitation.[113]

It is not clear whether and how the use of social media alone is captured in this definition. The SEC has issued little guidance as to this issue, and case law provides few clues. In their administrative proceeding against Prescient Capital Partners, Ltd. (PCP), the SEC found as a matter of fact that PCP used mail, email, social media, internet websites, and video to generally solicit investors.[114] This implies that the SEC believes social media can constitute a general solicitation. Unfortunately, the SEC does not describe the particular behavior on social media that constituted the solicitation. The SEC's cease-and-desist letter simply orders PCP "[to] cease and desist from committing or causing any violations and any future violations of Sections 5(a) and (c) of the Securities Act" (and pay fines).[115] Issuers have almost no evidence on whether the SEC will

111. Use of Electronic Media for Delivery Purposes, Securities Act Release No. 7233 (Oct. 6, 1995) (discussing inconsistencies in the placement of offering materials on the Internet with the prohibition against general solicitations or advertising).

112. IPOnet, SEC No-Action Letter, 1996 WL 431821, at *1 (July 26, 1996) (noting that investors could only access the information after being deemed "sophisticated").

113. *See* John C. Coffee Jr., *Brave New World?: The Impact(s) of the Internet on Modern Securities Regulation*, 52 BUS. LAW. 1195, 1221 (1997) ("Taken together, these three no-action letters both establish the concept that a password-protected Web site does not amount to a 'general solicitation' or 'general advertising' in violation of Rule 502. . . . ") (*citing* IPOnet, SEC No-Action Letter, 1996 SEC No-Act. LEXIS 642 (July 26, 1996); Angel Capital Electronic Network, SEC No-Action Letter, 1996 SEC No-Act. LEXIS 812 (Oct. 25, 1996); Lamp Technologies, Inc., SEC No Action Letter, 1997 SEC No-Act. LEXIS 638 (May 29, 1997)).

114. In the Matter of Prescient Capital Partners, Exchange Act Release No. 9363 (Sept. 24, 2012), https://www.sec.gov/litigation/admin/2012/33-9363.pdf [https://perma.cc/E2LW-J833] ("During the relevant period, Respondents made general solicitations of investors by means of mail, email, social media, and Internet websites and videos. These solicitations were prohibited by Rules 506(b)(1) and 502(c) of Regulation D."). Yet this does not make clear whether the social media solicitations alone would have been enough to violate the rules. Moreover, the fact-finding is obviously conclusory, as it provides no analysis as to whether social media is itself a general solicitation.

115. *Id.* (providing SEC orders pursuant to Section 8A of the Securities Act).

declare a social media behavior to be a general solicitation. Legal, socially valuable behavior may thereby be chilled needlessly.

2. Rule 504

When Rule 504 was first promulgated in 1982, it permitted the offer and sale of up to $500,000 in securities.[116] This limitation is statutorily required because Rule 504 is permitted under section 3(b) of the Securities Act, and section 3(b) expressly limits the SEC's authority for such permissive exemptions to specific dollar amounts.[117] That amount has been amended, however, and now it is presently $5 million.[118]

Rule 504 used to be relatively useless, but it was modified on October 26, 2016 in meaningful ways that made this exemption potentially quite useful.[119] As amended, Rule 504 now allows an offering of up to $5 million to an unlimited number of investors, whether accredited or not.[120] In addition, Rule 504 appears to permit limited public solicitation of investors.[121] While general solicitation is not permitted under Rule 504, the notion of a limited public solicitation makes this rule potentially quite powerful for social media investing.

Regulation D Rule 504 could be used to solicit investors for corporate financing on social media because it sidesteps the general solicitation ban. The leading treating on securities regulation states, "[a] general solicitation can be used for a Rule 504 offering if the transaction is registered under a state securities law that requires public filing and delivery of a substantive disclosure document."[122] In other words, Rule 504's power is limited, however, because compliance with this federal regulation does not preempt state securities regulations. Accordingly, a

116. *See* 17 C.F.R. § 230.504 (1984) (addressing the original limitation on offering price).

117. *See* Securities Act of 1933, ch. 38, § 3(b), 48 Stat. 74 (codified as amended at 15 U.S.C. §§ 77a-77aa); 17 C.F.R. § 230.504(a)(3) (2019) (noting the additional exemptions limiting the SEC's authority).

118. *See* 17 C.F.R. § 230.504(a)(3) (2019) (noting the amended amount exempt under section 3(b) of the Act).

119. *See* Exemptions to Facilitate Intrastate and Regional Securities Offerings, 81 Fed. Reg. 83,550, 2016 WL 6822600 (Nov. 21, 2016) (to be codified as 17 C.F.R. § 230.147, 230.147A) ("We also are adopting amendments to Rule 504 of Regulation D under the Securities Act to facilitate issuers' capital raising efforts and provide additional investor protections."); *see also SEC Adopts Final Rules to Facilitate Intrastate and Regional Securities Offerings*, SEC (Oct. 26, 2016), https://www.sec.gov/news/pressrelease/2016-226.html [https://perma.cc/NL3K-4EAS] (explaining the amendments to Rule 504).

120. Exemptions to Facilitate Intrastate and Regional Securities Offerings, 81 Fed. Reg. at 83,512 (discussing the allowance of a $5 million offering).

121. *See id.* ("Rule 504 imposes certain conditions, including limitations on the use of general solicitation or general advertising in the offering and the restricted status of securities issued pursuant to the exemption. . . .").

122. Hazen, *supra* note 110.

Rule 504 issuer under present law will also have to find an exemption for every state in which a purchaser resides.

Causing Rule 504 to preempt state securities regulation (also known as "blue sky laws") may be the killer feature necessary to make this exemption a powerful way for startup entrepreneurs to raise their first round of capital via social media. However, even without that change to the rules, Rule 504 is still marginally useful, as many states have an exemption for offerings to a limited number of purchasers when no general solicitation is involved, and a few states provide a state securities regulation exemption for issuances that otherwise comply with Rule 504.

Rule 504's power was further limited by its low fundraising limit, which was originally $500,000. Considering that the average venture capital investment into a startup company is $20.4M,[123] Rule 504 did not provide a viable alternative means of financing a startup. But the JOBS Act updated Rule 504 and increased its limit tenfold. Startups can now raise up to $5 million via this previously underutilized provision.

Given the newly enhanced power of Rule 504, it is more important than ever to understand whether social media posting constitutes a "limited public offering" or a "general solicitation." For example, Karen might be able to use social media to solicit investment in her startup thanks to Rule 504. South Dakota securities regulations provide an exemption to state registration for transactions that are exempt under the Securities Act of 1933.[124] If Karen has confidence about her ability to solicit investment in her new business to her friends from the Beacom School of Business via their Facebook group,[125] she might leverage social media to level the playing fields between herself and more well-connected entrepreneurs.

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123. NVCA 2020 YEARBOOK, NAT'L VENTURE CAPITAL ASS'N 32 (Mar. 2020), https://nvca.org/wp-content/uploads/2020/04/NVCA-2020-Yearbook.pdf [https://perma.cc/U7HH-4N2Q] (providing the average venture capital investment into a startup company).

124. *See* S.D. CODIFIED LAWS § 47-31B-202 (2020) (permitting certain transactions to be exempt from registration under the Securities Act of 1933 if:

(17) An offer to sell, but not a sale, of a security exempt from registration under the Securities Act of 1933 if:

> (A) A registration statement has been filed under this chapter, but is not effective;
>
> (B) A solicitation of interest is provided in a record to offerees in compliance with a rule adopted by the director under this chapter; and
>
> (C) A stop order of which the offeror is aware has not been issued by the director under this chapter and an audit, inspection, or proceeding that may culminate in a stop order is not known by the offeror to be pending.).

125. *USD Beacom School of Business Class of 2022*, FACEBOOK, https://www.facebook.com/groups/158389894785138/ [https://perma.cc/46SX-S578] (last visited July 28, 2020).

3. Rule 506

Originally, section 4(1) of the Securities Act of 1933 stated that the provisions of section 5 would not apply to "transactions by any issuer not with or through an underwriter and not involving any public offering."[126] The Securities Act has been amended since its inception and now it is section 4(a)(2) that declaims: issuers of securities are not required to register their transactions as long as they do not involve "any public offering."[127] As mentioned earlier, the SEC adopted Regulation D in 1982 as the "next logical step in the movement toward providing objective 'safe harbor' standards for, and clarifying the interrelationship of, the elements of the private and limited offering exemptions."[128] Purchasers receive "'restricted securities' through Rule 506 transactions that cannot be sold for a minimum of six months or a year without registering them."[129]

Until 1996, issuers seeking an exemption under federal securities regulations via Regulation D, if granted, were historically not protected from individual states' blue sky laws. For fourteen years, privately funded companies were required to comply with federal *and* state securities laws when attempting to raise capital in the United States. Congress addressed this disparate impact with the National Securities Markets Improvement Act (NSMIA), amending section 18 of the Securities Act to preempt state securities laws.[130] The NSMIA states: "no law, rule, regulation, or order, or other administrative action of any State or any political subdivision thereof . . . shall directly or indirectly apply to a . . . covered security."[131] Section 18(b)(4)(D) stipulates that "a security is a 'covered security' with respect to a transaction that is exempt from registration pursuant to commission rules or regulations issued under § 4(2) of the Securities Act of 1933."[132] Therefore, as long as an issuer meets the Rule 506 requirements in regard to "any public offering," that offering will be exempt from registration under federal securities laws in addition to being

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126. James M. Landis, *Legislative History of the Securities Act of 1933*, 28 GEO. WASH. L. REV. 29, 41 (1959) (discussing transactions section 5 provisions would not apply to).

127. 17 C.F.R. § 230.506(b) (2019) (noting under what circumstances issuers of securities are not required to register their transactions).

128. Theodore Parnall, Bruce R. Kohl & Curtis W. Huff, *Private and Limited Offerings After a Decade of Experimentation: The Evolution of Regulation D*, 12 N.M. L. REV. 633, 634 (1982) (discussing SEC adoption of Regulation D).

129. *Fast Answers: Rule 506 of Regulation D*, SEC (Nov. 27, 2017), https://www.sec.gov/fast-answers/answers-rule506htm.html [https://perma.cc/K828-9D3M] (providing when restricted securities may be sold).

130. *See* National Securities Markets Improvement Act of 1996, Pub. L. No. 104-290, Stat. 3416 (outlining the scope of exemptions from state regulation of securities offerings).

131. Securities Act of 1933, § 18, ch. 38, 48 Stat. 74 (discussing covered securities).

132. Hamby v. Clearwater Consulting Concepts, LLP, 428 F. Supp. 2d 915, 918 (E.D. Ark. 2006); *see also* Securities Act of 1933, § 18(b)(4)(D) (providing said statute).

exempt from state regulations for being "covered securities." The issuer will only be required to file its Form D.

a. Rule 506(b)

Rule 506(b) is the most frequently used exemption in securities regulation. Historically, over 99% of private placements were performed under Rule 506(b).[133] It is not an overstatement, therefore, to suggest that the enactment of Rule 506(b) is a key reason for the growth and development of the venture capital industry in the United States. Indeed, venture capital firms deployed over $1.7 trillion in investment via Regulation D Rule 506(b) in 2017.[134]

With the ability to remain outside the regulatory authority of both federal and state securities laws, it goes without saying that Rule 506 is an exceptionally powerful exemption. It currently allows an issuer to raise an unlimited amount of capital.[135] And Rule 506 permits fundraising from an unlimited number of "accredited investors" and up to thirty-five "other purchasers."[136] The caveat, however, is that issuers claiming the 506(b) exemption are not permitted to offer securities through any form of general solicitation or advertising.[137]

b. Rule 506(c)

When Title II of the JOBS Act took effect on September 23, 2013, the general solicitation ban was lifted—at least with regard to accredited investors—and Rule 506(c) was born.[138] Since its inception, over $2.5 trillion in capital has been raised via Rule 506(c).[139] Rule 506(c) is the

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133. Scott Bauguess, Rachita Gullapalli, & Vladimir Ivanov, *Capital Raising in the U.S.: An Analysis of the Market for Unregistered Securities Offerings, 2009–2017*, DIVISION OF ECONOMIC AND RISK ANALYSIS (DERA) U.S. SEC, 2 (Aug. 2018), https://www.sec.gov/files/DERA%20white%20paper_Regulation%20D_082018.pdf [https://perma.cc/ZGY2-PCAC] (discussing the frequency of the Rule 506(b) exemption).

134. *Id.* at 16, tbl. 3.

135. 17 C.F.R. § 230.506 (2019) (providing an issuer may raise an unlimited amount of capital).

136. *See Fast Answers: Rule 506 of Regulation D*, *supra* note 129. ("The company may sell its securities to an unlimited number of 'accredited investors' and up to 35 other purchasers.").

137. *Id.* (discussing what issuers are not permitted to offer when claiming the 506(b) exemption).

138. Tanya Prive, *General Solicitation Ban Lifted Today - Three Things You Must Know About It*, FORBES (Sept. 23, 2013), https://www.forbes.com/sites/tanyaprive/2013/09/23/general-solicitation-ban-lifted-today-three-things-you-must-about-it/#6333d107efa6 [https://perma.cc/JME3-U623] (discussing how the general solicitation ban was lifted, and implications of such a lift); *see also Eliminating the Prohibition on General Solicitation and General Advertising in Certain Offerings*, SEC (July 10, 2013), https://www.sec.gov/news/press/2013/2013-124-item1.htm [https://perma.cc/9TL5-4NNL] (providing that Ford D contains a separate box for issuers to check so that they may claim the 506 exemption that would permit general solicitation).

139. Bauguess, Gullapalli & Ivanov, *supra* note 133 at 16, tbl. 3.

product of the JOBS Act's mandate for the removal of the general solicitation ban that historically, and presently, restricts Rule 506(b).[140] Now, issuers may "broadly solicit and generally advertise an offering," so long as they "take reasonable steps" to verify that all of the purchasers are accredited and comply with the other conditions set forth in Regulation D.[141]

D. Regulation Crowdfunding

In addition, recent regulatory changes have attempted to make other exemptions more powerful and especially useful for nontraditional entrepreneurs who are not typical recipients of venture capital funding. Thanks to Title III of the JOBS Act of 2012, entrepreneurs could raise venture capital through equity crowdfunding portals starting in 2015.[142] In contrast to Regulation D offerings, however, "Reg CF" equity crowdfunding campaigns raised a total of $75.8 million in 2018.[143]

The relatively small use of equity crowdfunding results from many factors, including the fact that issuers must expend significant up-front costs prior to listing.[144] There is not yet a provision for permitting equity crowdfunding investors to resell their securities, and this creates an impediment to purchasing them in the first place.[145] In addition, it is difficult to form syndicates under Reg CF because the law does not permit investors to form special purpose vehicles (SPVs) or special purpose entities (SPEs).[146] These obstacles will have to be addressed if equity

140. *See* Jumpstart Our Business Startups Act, Pub. L. No. 112-106, § 201, 126 Stat. 313–14 (2012) ("The Securities and Exchange Commission shall revise its rules issued in section 230.506 of title 17, Code of Federal Regulations, to provide that the prohibition against general solicitation or general advertising contained in section 230.502(c) of such title shall not apply to offers and sales of securities made pursuant to section 230.506. . . .").

141. *General Solicitation – Rule 506(c)*, SEC, https://www.sec.gov/smallbusiness/exemptofferings/rule506c [https://perma.cc/XS4X-8PFD] (Mar. 12, 2020).

142. Press Release, SEC, SEC Adopts Rules to Permit Crowdfunding (Oct. 30, 2015), https://www.sec.gov/news/pressrelease/2015-249.html [https://perma.cc/H5T8-32V7].

143. Max Crawford, *Equity Crowdfunding 2018 Review*, START ENGINE INDEX (Jan. 14, 2019), https://www.startengine.com/blog/equity-crowdfunding-2018-review/ [https://perma.cc/7VXN-CAXM].

144. *See* Seth C. Oranburg, *Bridgefunding: Crowdfunding and the Market for Entrepreneurial Finance*, 25 CORNELL J.L. & PUB. POL'Y 397, 428 (2015) (discussing the many expenses issuers face before being listed).

145. *See* Seth C. Oranburg, *Democratizing Startups*, 68 RUTGERS U.L. REV. 1013, 1015 (2016) (explaining how staying private would not accomplish the goals of the JOBS act because of the inability of new, smaller investors to resell).

146. The challenge presented by Reg CF's restriction against SPVs has been recognized by members of Congress such as Patrick McHenry, Ranking Member of the Committee on Financial Services, who wrote a letter to that effect to the SEC on October 15, 2019. Letter from Patrick McHenry, Ranking Member, Comm. on Fin. Serv., to Vanessa Countryman, Secretary, SEC (Oct. 15, 2019), https://www.sec.gov/comments/s7-08-19/s70819-6293559-193383.pdf

crowdfunding is to make a meaningful impact on access to capital.[147]

Yet crowdfunding has made one very important contribution to new venture finance: democratization. Research has shown that female entrepreneurs receive a remarkably higher percentage of crowdfunding dollars than venture capital dollars.[148] Although equity crowdfunding is in its infancy, and studies on it are inherently preliminary, further research may show that securities exemptions that permit general solicitation are more "democratic" in that entrepreneurs of all races, genders, and geographies have more equal access to capital formation.

E. Regulation A

Title IV of the JOBS Act required the SEC to revise Regulation A in order to make larger amounts of capital available to medium-sized companies that could not afford the process of registering with the SEC and going public in an initial public offering (IPO).[149] The revised rule is colloquially referred to as "Reg A+" and has two offering tiers with different requirements depending on the amount of funding raised.[150]

Tier 1 offerings are for fundraisings up to $20 million.[151] If the offeror stays under this limit for a twelve-month period, the offeror may sell stock to the general public.[152] It does not limit the offering to accredited investors only. Additionally, it permits the offeror to generally solicit the offering to the public via a website such as the ports described below. However, Reg A Tier 1 offerings have a fatal flaw: they do not offer preemption from state blue sky laws. As a result, a Reg A+ Tier 1 issuer will have to comply with the blue sky laws in every state in which a purchaser resides.

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147. Legislation has been proposed that would address some of these concerns; however, the Fix Crowdfunding Act, H.R. 4855, has not seen action since its amended version passed the House on July 5, 2016. Fix Crowdfunding Act, H.R. 4855, 114th Cong. (2016).

148. MARK GEIGER & SETH ORANBURG, RESEARCH REPORT PRESENTED AT BABSON COLLEGE, DO FEMALE INVESTORS SUPPORT FEMALE ENTREPRENEURS? AN EMPIRICAL ANALYSIS OF ANGEL INVESTOR BEHAVIOR, (2019) https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3429077 [https://perma.cc/9TPH-BVW9].

149. *See* Securities Act of 1933, §§ 3, 4, 18, ch. 38, 48 stat. 74 (codified as amended at 15 U.S.C. §§ 77a–77aa); Pub. L. 112-106, 126 Stat 323–24, §§ 401–402 (2012); 17 C.F.R. §§ 230.251–230.263 (2020) (detailing the SEC revisions made to Regulation A).

150. *See* 17 C.F.R. § 230.251 (2019) (setting out the two offered tiers); *see also* Daniel Huang, *Small Crowds Get Their Day in Investing Sun*, WALL ST. J. (June 18, 2015), https://www.wsj.com/articles/small-crowds-get-their-day-in-investing-sun-1434655720 [https://perma.cc/JN4Q-8TFX (discussing the potential impact the new rules will have in democratizing how new entrepreneurs raise funds).

151. 17 C.F.R. § 230.251(a)(1) (2019); *see also Regulation A*, U.S. SEC. & EXCHANGE COMM'N, https://www.sec.gov/smallbusiness/exemptofferings/rega [https://perma.cc/LM4R-CGZR] (last visited May 25, 2020) (summarizing the important points of Regulation A for small businesses).

152. 17 C.F.R. § 230.251(a)(1) (2019).

This limitation is particularly problematic in a social media world. A key reason to use social media to solicit potential investors is to reach investors across the nation or even the world.[153] Social media is as geographically unbounded as the internet itself.[154] But such an unbounded offering would require the issuer to be prepared to comply with securities regulations in virtually every state. This greatly adds to the complexity of such an offering. Indeed, the lack of blue sky preemption is often cited as the reason why the original Regulation A did not work.[155]

Reg A Tier 2, on the other hand, permits general solicitation to nonaccredited investors and provides preemption from state blue sky laws.[156] Blue sky law preemption is considered to be one of the most significant benefits of this exemption.[157] In addition, it permits fundraising up to $50 million from nonaccredited investors.[158] These are significant benefits that make Tier 2 offerings more attractive. Indeed, Reg D Tier 2 offerings are especially useful as a "mini-IPO" through which companies can raise up to $50 million and thereby "test the waters" as to whether they would succeed in a full-blown IPO.

Tier 2 offerings also have significant additional costs. First, companies engaged in Tier 2 offerings must produce a detailed statement that includes two years of audited financials.[159] The company must wait for

153. *See, e.g.*, Alejandro Cremades, *How to Use Social Media to Pitch Investors*, FORBES (Mar. 5, 2019, 9:55 AM), https://www.forbes.com/sites/alejandrocremades/2019/03/05/how-to-use-social-media-to-pitch-investors/#736466b11dd8 [https://perma.cc/B8QC-FAQC] (discussing ways in which startup entrepreneurs can utilize social media to connect with potential investors).

154. *See, e.g.*, Esteban Ortiz-Ospina, *The Rise of Social Media*, OUR WORLD IN DATA (Sept. 18, 2019), https://ourworldindata.org/rise-of-social-media [https://perma.cc/8GUN-2ERU] (comparing the 3.5 billion people globally using social media of some form with the 7.7. billion global population); Dave Chaffey, *Global Social Media Research Summary 2020*, SMART INSIGHTS (Aug. 3, 2020), https://www.smartinsights.com/social-media-marketing/social-media-strategy/new-global-social-media-research/ [https://perma.cc/W7M4-SEU4] (breaking down global social media usage by platform); *Social Media Statistics and Facts*, MARKETS.US, https://market.us/statistics/social-media/ [https://perma.cc/6U9W-C4YY] (Apr. 17, 2020) (comparing social media usage by global region).

155. *See, e.g.*, Rutherford B. Campbell Jr., *Blue Sky Laws and the Recent Congressional Preemption Failure*, 22 J. CORP. L. 175, 193–94 (1997) (discussing how state regulations undercut the usefulness of the original version of Regulation A).

156. 17 C.F.R. § 230.251 (2019); *see* John A. Aiello & Philip D. Forlenza, *Regulation A Plus: A New Tool to Raise Capital*, N.J. LAW. 11, 13 (2015) ("Tier 2 offerings are not subject to any type of state law review, and are federally preempted under Regulation A Plus because a purchaser in a Tier 2 offering is considered a qualified purchaser."); Amendments for Small and Additional Issues Exceptions under the Securities Act (Regulation A), Securities Act Release Nos. 33-9741; 34-74578; 39-2501 (Mar. 25, 2015).

157. Christian W. Borek, *Regulation A+: Navigating Equity-Based Crowdfunding under Title IV of the JOBS Act*, 47 CUMB. L. REV. 143, 168 (2016).

158. 17 C.F.R. § 230.255(a) (2019).

159. *See* 17 C.F.R. § 230.257(b)(2) (2019) (detailing the requirements that an issuer engaged in Tier 2 offerings needs to file with the SEC).

the SEC to review and comment on the offering statement before making the stock offering.[160] After the stock offering, Tier 2 companies continue to have reporting obligations; annual and semiannual reports must be posted to the SEC's database, EDGAR, where anyone can view them.[161]

These costs and benefits make Tier 2 offerings more analogous to mini-IPOs than to upgraded Tier 1 offerings. Tier 1 offerings are themselves more like upgraded Rule 504 offerings, in that both of these allow sales of stock to nonaccredited investors on a federal level but do not provide preemption from state blue sky laws. Tier 2 offers are like a downsized IPO. Both the IPO and the mini-IPO require periodic reporting and publication of risk factors and audited financials on EDGAR, and both provide preemption from state securities regulations. A Tier 2 issuer can even list on a stock public exchange like the NASDAQ or NYSE, so long as it complies with the requirements thereto under the Securities Exchange Act of 1934.[162]

Reg A Tier 2 has indeed found its niche as a way for many pre-IPO companies to "test the waters" and determine whether they are good candidates for an IPO without investing the massive resources to go through the full-blown IPO process.[163] The proof of its utility is in the numbers. From July 19, 2015 (when the new rules governing Reg A came into effect) to December 31, 2018, there were 115 companies who raised $1.27 billion via Tier 2.[164] During that same time period, only 42 companies raised $230 million via Tier 1.[165]

F. Regulation S

This Article's scope is limited to securities regulation in the United States. However, it bears brief mention that as investing goes online, geographic boundaries begin to break down. This is especially true of cryptocurrency investments, which may not even be traceable by

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160. *Investor Alerts and Bulletins: Updated Investor Bulletin: Regulation A*, SEC (May 24, 2019), https://www.sec.gov/oiea/investor-alerts-bulletins/ib_regulationa.html [https://perma.cc/772C-ST2K] ("For Tier 2 offerings, the offering circular is subject to review and *qualification* by the staff at the SEC, but is not subject to review by state securities regulators. Financial statements disclosed in a Tier 2 offering must be audited by an independent accountant.").

161. *See* 17 C.F.R. §§ 230.257(b)(1), 230.257(b)(3) (2019) (identifying the obligations Tier 2 companies continue to have post-stock offering); *see also About EDGAR*, SEC, https://www.sec.gov/edgar/about [https://perma.cc/9QVB-C2W9] (May 27, 2020) (summarizing the general purpose and operations of EDGAR as the SEC's reporting system).

162. Bonnie J. Roe, *Will Regulation A+ Find Its Niche? Some Opportunities to Explore*, BUS. L. TODAY 1, 2 (2015).

163. Borek, *supra* note 157, at 164–66.

164. Rod Turner, *These 107 Companies Raised $1.5 B via Regulation A+; New Metrics*, MEDIUM (June 5, 2019), https://medium.com/@IamRodTurner/these-107-companies-raised-1-5-b-via-regulation-a-new-metrics-7b60ec41958b [https://perma.cc/B7JK-K5QP].

165. *Id.*

domestic securities regulators. Regulation S provides an exemption for companies to raise capital outside the United States.[166] This "safe harbor" applies where no offering participant has engaged in any "directed selling efforts" in the United States.[167] This Article regards the use of social media to solicit the sale of securities to U.S. persons. Whether or to what extent social media outreach could be made without any effort toward or impact upon U.S. persons is beyond the scope of this Article.

III. SOCIAL MEDIA INVESTMENT PLATFORMS

The enactment of the JOBS Act and the resulting promulgations by the SEC of Rule 506(c), Reg A+, and Reg CF have given rise to a new type of social media platform: the social media investment platform. This part will explore the nature of these platforms. At the outset, it is important to note that all the recently developed platforms employ features for users such as groups, following, likes, message boards, direct messaging, and other communication tools commonplace in standard social media applications.

A. Angel Investment Portals

Recall that Rule 506(c) requires "reasonable steps" to verify that all the purchasers are accredited.[168] Those reasonable steps may require an issuer to be more invasive with regard to determining an investor's status. For example, the issuer may have to verify the investor's income or wealth by obtaining a copy of their tax filings or bank statements.[169] Perhaps because it is more efficient for investors to be scrutinized fewer times by a centralized authority, this new rule has led to the emergence of a new type of investment portal on the internet. Rule 506(c) "angel

166. 17 C.F.R. §§ 230.901–905 (2019).

167. 17 C.F.R. § 230.903 (2019).

168. *See Fast Answers: Rule 506 of Regulation D*, *supra* note 129 (summarizing Rule 506 of Regulation D for investors).

169. *Eliminating the Prohibition Against General Solicitation and General Advertising in Rule 506 and Rule 144A Offerings*, SEC, https://www.sec.gov/info/smallbus/secg/general-solicitation-small-entity-compliance-guide.htm [https://perma.cc/D7JU-Z5F6] (Sept. 20, 2013).

investment" portals including AngelList,[170] OurCrowd,[171] Gust,[172] and SeedInvest[173] have emerged to service accredited investors who want to discover investment opportunities and invest online. Individuals issuing securities to companies via these platforms do not have to verify an investor's accredited status because the portal has already done so on their behalf.[174]

These portals generally offer features for users commonly used in standard social media applications.[175] For example, on AngelList, you can "follow" investors including celebrities like Ashton Kutcher.[176] In fact, the "syndicated" nature of investment on AngelList is its most striking feature, as described in the next section. OurCrowd hosts live streaming web events so investors from around the world can attend

170. Home Page, ANGELLIST, https://angel.co/ [https://perma.cc/XQ7T-X2XR] (last visited July 28, 2020).

171. "OurCrowd is a global crowd investing platform for accredited investors. It sources deals, performs due diligence, and opens investments to its members, leading every investment with its own money. It takes an active stake in the companies it finances, through board seats and a mentorship program that pairs startups with OurCrowd contacts from relevant industries." As of September 2020, OurCrowd and its investor community have invested more than $112.50M for 100+ companies and funds. *OurCrowd - Crunchbase Company Profile & Funding*, CRUNCHBASE, https://www.crunchbase.com/organization/ourcrowd#section-overview [https://perma.cc/B84L-N4MD] (last visited Aug. 17, 2020).

172. "Gust is the global platform for founding, incorporating and operating scalable, high growth companies. It leverages that position—and Gust's allied platform for investment organizations—to enable the early-stage investing ecosystem. Gust's knowledge and collaboration tools support all aspects of corporate legal and equity formation, operation and funding for entrepreneurs from startup to exit." *Gust - Crunchbase Company Profile & Funding*, CRUNCHBASE, https://www.crunchbase.com/organization/gust#section-overview [https://perma.cc/L2T9-6GN2] (last visited Aug. 17, 2020).

173. "SeedInvest is an equity crowdfunding platform that provides investors with access to highly vetted startup investment opportunities. The SeedInvest network contains over 15,000 accredited investors, including hundreds of family offices and institutions. SeedInvest typically invests between $500,000 – $5 million as part of a syndicate." *SeedInvest – Crunchbase Investor Profile & Funding*, CRUNCHBASE https://www.crunchbase.com/organization/seedinvest#section-overview [https://perma.cc/7DED-87SE] (last visited Aug. 17, 2020).

174. For example, AngelList employs a team of lawyers and CPAs who review prospective investors' financial information in order to verify that they meet the definition of "accredited investors" pursuant to Regulation D. *Investor Accreditation*, ANGELLIST, https://angel.co/help/accreditation [https://perma.cc/63C9-DJ5H] (last visited July 28, 2020).

175. Social network sites are defined as web-based services that "allow individuals to (1) construct a public or semi-public profile within a bounded system, (2) articulate a list of other users with whom they share a connection, and (3) view and traverse their list of connections and those made by others within the system. The nature and nomenclature of these connections may vary from site to site." Danah M. Boyd & Nicole B. Ellison, *Social Network Sites: Definition, History, and Scholarship*, 13 J. COMPUTER-MEDIATED COMM. 210, 211 (2008), https://onlinelibrary.wiley.com/doi/pdf/10.1111/j.1083-6101.2007.00393.x [https://perma.cc/U4MJ-KWLL].

176. *Ashton Kutcher Profile*, ANGELLIST, https://angel.co/aplusk [https://perma.cc/6UN4-VG9L] (last visited Aug. 17, 2020).

virtual summits together.[177] Gust provides investors with communication tools that allow them to discuss, track, review, and share information about deals.[178] SeedInvest allows potential investors to message companies directly or post questions to the company's discussion board that all potential investors can see.[179]

All these platforms have a rigorous process for determining whether a user is "accredited." Throughout its site, AngelList states "[y]ou must be an accredited investor to invest on AngelList."[180] AngelList further requires investors to go through a ten-minute application process, which requires users to answer financial questions, provide links to online profiles, write narratives about investment experience, and certify to the following:

- I indemnify AngelList and understand that most startups lose investors' money.
- I understand that AngelList doesn't verify information on the site, and I'm responsible for diligence.
- If I invest, I will use an attorney and comply with securities laws.
- I will be permanently banned from AngelList if I falsely represent my accreditation status.[181]

AngelList then spends up to a week reviewing each application. AngelList reserves the right to request additional information or to deny access. This is the most rigorous investor review process encountered during the research for this Article.

Such social network features are particularly useful for the formation of investment syndicates. A syndicate is a group of investors who follow a lead investor.[182] The lead investors are responsible for sourcing the deal, performing due diligence, negotiating the terms, and managing the closing. Sometimes, the lead obtains a seat on the company's board in

177. *Livestream: Watch the Summit Live from Anywhere*, OURCROWD SUMMIT, https://summit.ourcrowd.com/livestream/ [https://perma.cc/UUN8-U6DC] (last visited Aug. 17, 2020).

178. *Investors*, GUST, https://gust.com/investors [https://perma.cc/B85E-569A] (last visited Aug. 17, 2020).

179. *FAQs*, SEEDINVEST, https://www.seedinvest.com/faqs [https://perma.cc/AN8Z-NADN] (last visited Aug. 17, 2020).

180. *Syndicates for Investors*, ANGELLIST, https://angel.co/syndicates/for-investors [https://perma.cc/PX4V-4PSA] (last visited Aug. 17, 2020); *AngelList Help: What is an Accredited Investor?*, ANGELLIST, https://help.angel.co/article/747-what-is-an-accredited-investor [https://perma.cc/4KWE-3HUY] (last visited Aug. 17, 2020).

181. *Account Creation Page*, ANGELLIST, https://angel.co/join?source=homepage&source_content=global_header_join_text [https://perma.cc/9GWS-H2B7] (last visited Aug. 17, 2020).

182. *See Syndicates*, ANGELLIST, https://angel.co/syndicates [https://perma.cc/G3RE-DBZ3] (last visited May 27, 2020) (providing the definition of a syndicate).

order to ensure that the company continues to serve the investors' interests. In exchange for these efforts, the lead sometimes receives what is referred to as the "carry," which is a percentage commission on the profits from the deal.[183]

Syndicates are very important for investing because they can increase efficiency. Instead of each investor doing diligence for themselves, which would result in a massive duplication of efforts when multiple investors are involved, a single person can be trusted with this task. The lead investor is often the one with the most experience and resources and so is the least cost avoider[184] for this job. Follow-on investors can trust that the lead will perform diligence dutifully because the carried interest that the lead earns if the deal is profitable is expected to further motivate the lead to take care. This also simplifies negotiations because the company can negotiate with the lead alone rather than with several counterparties.

AngelList focuses on syndicates for its investments, and syndicates on AngelList are private groups. To join a syndicate, an investor needs to apply to the lead investor. AngelList has over 200 syndicate leads—experienced angel investors who (presumptively) have vetted target investments. Leads share details about investment opportunities with their followers, who typically have five business days to decide whether to invest.

B. Equity Crowdfunding Portals

Remember that entrepreneurs were permitted to raise funds through equity crowdfunding portals starting in 2015.[185] The most popular of those portals is currently WeFunder.com, which funded $25.8 million in 2018.[186] Upon signing up for WeFunder, it becomes immediately apparent that the platform takes a very social approach to crowdfunding. It first asks the new user to upload a picture and to connect your Facebook, LinkedIn, Twitter, and AngelList account. Another crowdfunding portal, MicroVentures, permits the user to sign up directly

183. Jo Tango, *How are VC's Paid?*, JTANGO VC (Mar. 2, 2012), https://jtangovc.com/how-vcs-are-paid/ [https://perma.cc/5CFP-BTV3].

184. The least-cost avoider is the party who has the lower cost of avoiding harm. In tort law, the least-cost avoider principle is the assignment of liability to the party who has the lowest cost of avoiding harm. *See* Eric Rasmusen, *Agency Law and Contract Formation*, 6 AM. L. & ECON. REV. 369, 380 (2004) (further explaining the "Least-Cost Avoider" principle).

185. *See* Prive, s*upra* note 138 (announcing that startups are now able to publicly advertise that they are seeking investment during startup fundraising).

186. Brian Thopsey, *The Top 10 Equity Crowdfunding Portals 2019*, FUNDWISDOM (Nov. 3, 2019), https://fundwisdom.com/article/brian-thopsey/top-10-equity-crowdfunding-portals-2019 [https://perma.cc/6ZJX-ACHD].

through other social media applications such as Twitter or Google+.[187]

WeFunder then asks the user to indicate his or her skills, such as engineering or finance, and to answer some questions such as "how do you think we can fix America?" It is a bit quirky in this regard, asking, for example, "[w]hat is your post apocalyptic [*sic*] survival skill?"[188] The answers to these questions are shared with other users, presumptively to make the experience more human and social.

WeFunder users are asked to select from a list of interests that range from minority-owned businesses, "mainstreet" small businesses, space travel, moonshots,[189] alcohol, artificial intelligence, and sustainability.[190] The range of these topics implies that WeFunder users are impact investors or even venture philanthropists.[191] An impact investor is one who cares about the "triple bottom line": people, planet, and profit.[192] Impact investors are seen on non-equity crowdfunding platforms,[193] where social effects like homophily (the tendency to associate and bond with similar others)[194] motivate investors to contribute to projects.[195] If equity crowdfunding users are motivated to invest by the same principles

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187. *Account Login Page*, MICROVENTURES, https://app.microventures.com/account/login [https://perma.cc/YU28-99N2] (last visited Aug. 17, 2020).

188. *Invest in Startups You ♡*, WEFUNDER, http://wefunder.com/welcome (select sign up and create a profile) [https://perma.cc/B4YG-RDFB] (last visited Aug. 13, 2020).

189. A moonshot is an extremely difficult task, the pursuit of which may seem crazy. *See* Alex Davies, *Why 'Moon Shot' Has No Place in the 21st Century*, WIRED (July 16, 2019, 7:00 AM), https://www.wired.com/story/apollo-11-moonshot-21st-century/ [https://perma.cc/67ZE-624C] ("Fifty years after Neil Armstrong walked on the moon, planted an American flag, and flew home, the term *moon shot* has become shorthand for trying to do something that's really hard and maybe a bit crazy.") (emphasis in original).

190. MicroVentures similarly asks what industries the user is interested in, such as "clean tech," "financial tech," "educational tech," "local businesses," and/or "media/entertainment." *See* MICROVENTURES, *supra* note 187 (asking users to denote their preferences while creating an account).

191. *See* Seth C. Oranburg, *Start-Up Financing 2.0* (Mar. 6, 2016; 2d Ed. forthcoming 2021) at 15–16, https://ssrn.com/abstract=2743072 [https://perma.cc/HGF7-9DPG] (defining venture philanthropy and impact investing and explaining their role in start-up financing).

192. *See Our Story*, SUSTAINABILITY, https://sustainability.com/who-we-are/our-story/ [https://perma.cc/YFZ2-WTGL] (last visited Aug. 13, 2020) (providing the origin story and philosophy of SustainAbility, whose founder coined the term "triple bottom line"); *see also Triple Bottom Line*, ECONOMIST (Nov. 17, 2009) https://www.economist.com/news/2009/11/17/triple-bottom-line [https://perma.cc/CU2R-EXCG] (defining the three "lines" of the triple bottom line).

193. *See, e.g.*, Jason Greenberg & Ethan Mollick, *Activist Choice Homophily and the Crowdfunding of Female Founders*, 62 ADMIN. SCI. Q. 341, 357–58 (2017) (examining the extent to which female founded companies are funded through donation-based crowdfunding).

194. *See* Barbara S. Lawrence & Neha Parikh Shah, *Homophily: Measures and Meaning*, 2 (UCLA Working Paper 2017) (defining homophily).

195. *See* Jason Greenberg & Ethan Mollick, *Leaning In or Leaning On? Gender, Homophily, and Activism in Crowdfunding*, ACAD. MGMT. PROCEEDINGS 1, 1–2 (July 2014) ("[A] small proportion of female investors disproportionately support women-led projects in areas where women are historically underrepresented.").

that apply to non-equity crowdfunders—such as social cohesion, a sense of belonging, desire for acceptance, and helping similar others—then it is unsurprising that equity crowdfunding platforms would heavily utilize social media devices, as WeFunder does.

WeFunder then asks the user financial questions that are relevant to determine how much the user is permitted to invest each year on equity crowdfunding. It also requires the user to check several boxes acknowledging the risks of equity crowdfunding. To proceed, the user must answer yes to "I understand securities on WeFunder are not easily resold. There is no secondary market. I can wait years for a return."[196]

Notably, the author was able to register for WeFunder as an "accredited investor" simply by dragging the "net wealth" slider to "1 million."[197] WeFunder did not ask for any verification of income or assets before allowing the author to proceed to research and invest in companies.[198] Other crowdfunding portals, like EquityZen,[199] were slightly more stringent, requiring the user to check a box stating: "I understand that I may be permanently banned from EquityZen if I provide false information relating to my status as an accredited investor."[200]

On the other end of the spectrum, MicroVentures states that "[y]ou do not have to be an accredited investor to invest on the MicroVentures platform"; however, "accredited investors may have access to additional investment opportunities."[201] Notably, WeFunder is not restricted to only accredited investors either, and they boast that anyone can "invest as little as $100 in startups and small businesses."[202] WeFunder does admit that

196. In prior work, this Article's author explained how the lack of a resale market for crowdfunding securities could chill interest in purchasing these securities in the first place. *See* Oranburg, *supra* note 145, at 1013 (recommending a new "Rule 144B" that would permit the resale of crowdfunded securities, much like Rule 144A permits the resale of private securities that were originally sold under Reg D.); *see also* 17 C.F.R. § 230.144A (2019) (defining rules regarding private resales of securities to institutions); *see also Open an Investor Account*, WEFUNDER, http://wefunder.com/welcome [https://perma.cc/B4YG-RDFB] (last visited Aug. 13, 2020)

197. *See* WEFUNDER, *supra* note 196 (guiding potential investors in creating an account); *see also Investor Verification Process*, WEFUNDER, https://wefunder.com/accredited/verification [https://perma.cc/B5RN-93MB] (last visited Aug. 13, 2020) (explaining the process by which WeFunder verifies potential investors' income and net worth).

198. However, there is a verification process that takes place within 48 hours of registering as an accredited investor. *Id.*

199. *The Marketplace for Pre-IPO Equity*, EQUITYZEN, https://equityzen.com [https://perma.cc/97XS-53G5] (last visited Aug. 13, 2020).

200. *Are you an accredited investor?*, EQUITYZEN, https://equityzen.com/investor/access [https://perma.cc/Y6HU-K7CF] (last visited Aug. 17, 2020); *How to Know if You're an Accredited Investor*, EQUITYZEN, https://equityzen.com/knowledge-center/newsletter/how-to-know-if-youre-an-accredited-investor/ [https://perma.cc/CH93-TWTJ] (last visited Aug. 13, 2020).

201. MICROVENTURES, *supra* note 187.

202. *Investor Relations*, WEFUNDER, https://wefunder.com/jobs/support [https://perma.cc/537N-MYR2] (last visited Aug. 13, 2020).

"it's complicated" and "when you sign up for a WeFunder account, [WeFunder will] do all these calculations for you."[203]

The WeFunder interface is quite different from AngelList,[204] and MSC,[205] in that WeFunder focuses on "trending" companies.[206] This once again reinforces the social dimension of this platform. Companies are featured more prominently as users "heart" campaigns.[207] Each campaign has its own promotional page. WeFunder focuses heavily on the identity of the founder with images and videos of the founders talking about their product, whereas AngelList focuses on the identity of the other investors, and Manhattan Street Capital (MSC) focuses on the nature of the product and the financials.

C. Mini-IPO Portals

The most successful Reg A+ portal to date is MSC.[208] This platform focuses on mid-stage and mature companies.[209] MSC is a password-protected website but creating an account is simple—all that is needed is a username and password. Users do not have to provide any personally identifying information in order to browse the site. Offerings span many industries ranging from real estate, biologics, electric vehicles, and even novel golf products. Each offering has its own web page which generally features graphics and videos about the company, the product, and the team.

For example, MSC featured an opportunity to invest in GolfSuites 1, an investment company that develops hybrid-golf centers (like Top Golf) in the Midwest region.[210] Terms of the offering are listed as $5.20 per share with a minimum investment of $500.[211] There is a button on the

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203. *How Much am I Allowed to Invest?*, WEFUNDER, https://help.wefunder.com/legal/304304-how-much-am-i-allowed-to-invest [https://perma.cc/XDT3-3VNQ] (last visited Aug. 13, 2020).

204. *See infra* Section III.A (discussing the features of Angel investment portals).

205. *See infra* Section III.C (discussing the features of mini-IPO portals).

206. *See Invest in Startups You Love*, WEFUNDER, https://wefunder.com/explore [https://perma.cc/BB2T-VA8Y] (last visited Aug. 13, 2020) (allowing WeFunder users to sort through start-ups by various features, including whether the start-up is trending).

207. *See id.* (allowing WeFunder users to "heart" companies that interest them).

208. *See About Us*, MANHATTAN ST. CAP., https://www.manhattanstreetcapital.com/about-us [https://perma.cc/8VBT-VVEF] (last visited Aug. 13, 2020) (asserting that MSC supports investing through Reg D, Reg S, and even Security Token Offerings ("STOs") or Blockchain offerings).

209. *Id.*

210. *See GolfSuites 1*, MANHATTAN ST. CAP., https://www.manhattanstreetcapital.com/golfsuites [https://perma.cc/6F6G-2EPH] (last visited Aug. 13, 2020) (providing details regarding GolfSuites investment opportunity).

211. The share price was increased from $5.20 to $5.30 in an April 27, 2020, supplement to the offering. *Id.*; *see also GolfSuites Offering Circular Supplement*, MANHATTAN ST. CAP. (Apr. 27, 2020), https://www.manhattanstreetcapital.com/offering-circular/17483 [https://perma.cc/8782-AD5H] (reflecting share price changes).

promotional web page to "invest now," even before reading the offering circular.

Upon clicking "invest now," the user fills out a very simple form: how much to invest ($500 minimum), investor type (individual, company, or trust or IRA), legal name, email, phone, country and state of residence, and whether a U.S. citizen or a permanent resident. There is an optional field to indicate whether the user is an accredited investor. Beyond that, the user simply checks the box to confirm the information is correct, the user read the offering circular,[212] and that the user's annual income or savings is greater than $5000. MSC does not require the user to upload any documentation that would prove this is true.

On the second page, the user enters address and payment information. Debit cards, ACH, wire transfers, and personal checks are accepted. If the user selects personal check, a green "proceed" option appears, and the user thus enters into a legally binding transaction to purchase this stock, including a promise to pay for it via a check in the mail.

Investing with MSC is a remarkably simple process, but users can get more involved if they so choose. For example, users can write or read others' comments, "like" the offering, or send a message to the issuer asking questions. The user can also read the offering circular, which includes financial statements.[213]

Of all the portals mentioned, MSC emphasizes its social media content the least, but social media tools are still made available to MSC users. Upon clicking "comments," the user can view various posts from other users and replies which are generally made by the issuer's CEO. Quite frankly, many of the comments are unhelpful and potentially distracting. For example, on October 12, "Robert" commented that "Huge New Jersey and [New York] market thousands of [N]ew Yorkers come to the [P]oconos and spend lots of money also have lots of summer and winter homes here huge market maybe you should take a look then I would consider [i]nvesting contact me."[214] The CEO replied, "since this particular offering is for the midwest US, the NY/NJ area is not in the equation for now."[215] Obviously, Robert did not read the promotional

212. *GolfSuites Offering Circular Supplement*, MANHATTAN ST. CAP. (Feb. 21, 2020), https://www.manhattanstreetcapital.com/sites/default/files/GS1_OC_with_Supplements_02-21-2020.pdf [https://perma.cc/D8UA-JJTY].

213. *GolfSuites Offering Circular Supplement*, *supra* note 211 (this information is also accessible via a link on MSC's page for *GolfSuites 1*, *supra* note 210).

214. Robert, Comment to *GolfSuites 1*, MANHATTAN ST. CAP. (Oct. 12, 2019), https://www.manhattanstreetcapital.com/golfsuites [https://perma.cc/6F6G-2EPH].

215. Jerry Ellenburg, Reply to Robert's comment on *GolfSuites 1*, MANHATTAN ST. CAP. (Oct. 17, 2019), https://www.manhattanstreetcapital.com/golfsuites [https://perma.cc/6F6G-2EPH].

materials or the offering circular before posting this comment.[216]

It may also be the case that users are investing without reading these materials—a notion that the SEC surely would use to support the ban on general solicitation. Unsophisticated investors—ones that do not read or do not know how to read such investment materials—are the precise classification of individual the SEC is out to "protect" with the regulations described in this Article. The SEC's intentions may be pure and geared at improving social welfare at large, but at what cost? Should our goal be to protect unsophisticated investors from themselves, or can we build a regulatory regime that protects the vulnerable while simultaneously promoting the creation of wealth for people like Karen from rural Dallas, South Dakota?

D. Analysis of Investment Platforms

The three types of investment platforms described above—angel investor, equity crowdfunding, and mini-IPO—each have similar features. To a greater or lesser extent, they all use social media to engage users, they all require users to answer some basic financial questions, and they all source and promote investment opportunities. However, the differences are much greater than the similarities.

1. Investor Scrutiny

The first dimension in which these platforms vary is their degree of scrutiny of the user. The most scrutiny applies to angel investor platforms. From a legal perspective, this makes sense. The inclusion of even one nonaccredited investor in a financing that seeks to be exempt from registration pursuant to Reg D Rule 506(c) may lose its exempt status merely by soliciting a nonaccredited investor.[217] On the other end of the spectrum are the equity crowdfunding platforms. Although users had to check a few boxes certifying, for example, that they understand that the securities cannot be resold, it was not clear that an ordinary investor would pay attention to or understand these cautionary steps. Other platforms provide even less warning and go as far as advertising that you can invest as little as $100.[218] In general, the equity crowdfunding platforms have a more whimsical approach. The mini-IPO platforms are in the middle. Reg A+ does not require as much investor

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216. *See GolfSuites Offering Circular*, *supra* note 211 (providing updated and supplemental information regarding the GolfSuites investment opportunity).

217. *See* 17 C.F.R. § 230.506(c) (2019) (defining exemptions for limited offers and sales without regard to dollar amount of offering).

218. *See WeFunder FAQ*, WEFUNDER, https://help.wefunder.com/#/getting-started-for-founders [https://perma.cc/2CC4-MZM4] (last visited Aug. 13, 2020) (explaining that WeFunder does not require custodians for companies that offer investment contracts directly to every investor on WeFunder who invests as little as $100).

scrutiny as Reg D Rule 506(c) does, but the mini-IPO platforms had a serious look and feel.[219]

2. Financial Focus

The platforms also had a different degree of focus regarding finances. The mini-IPO platform was the most financially focused. The organization of the site, the presentation of the promotional materials, and the questions asked in the comments focused on matters related to risk (e.g., quality of product, competitors, background of managers) and return (e.g., prospects for an IPO, dividends, historical financial performance).[220] On the other end of the continuum was the equity crowdfunding platforms, which focused on other matters such as social impact, the founders' stories, community development, eco-friendly processes and other "feel-good" aspects that were not directly related to return on investment. The angel investment platforms were the middle of the road. AngelList predominately focused on the "lead" investor, whose reputation functioned as a sort of proxy for the issuer's financial potential.[221] OurCrowd's use of investor summits and video dialogue with management mixes financial acumen with the human element.

3. Offering Volume

The third way in which these platforms differ significantly is the volume of offerings that occur on these websites. By far, the angel crowdfunding platforms have the most volume of sales via the Reg D Rule 506(c) offerings. As mentioned above, Regulation D was and remains the most utilized exemption to securities registration

219. Websites can convey a serious or whimsical look and feel by choosing certain fonts, colors, and images. *See e.g.*, Ted Hunt, Infographic in *A Pro Designer Shares the Psychology of Font Choices*, THE DAILY EGG, https://www.crazyegg.com/blog/psychology-of-fonts-infographic/ [https://perma.cc/64B5-8BFP] (Oct. 21, 2019) (showing a visual representation of the emotions different fonts typically evoke); *see also* Nick Kolenda, *Font Psychology*, NICK KOLENDA PSYCH. & MKTG., https://www.nickkolenda.com/font-psychology/ [https://perma.cc/9NPP-22K3] (last visited Aug. 13, 2020) (explaining the "art and science" of choosing fonts). MSC's website conveys a serious tone by using sharp edged sans serif fonts that produce an impression of stability and objectivity. *See* Ted Hunt, *A Pro Designer Shares the Psychology of Font Choices*, THE DAILY EGG, https://www.crazyegg.com/blog/psychology-of-fonts-infographic/ [https://perma.cc/64B5-8BFP] (Oct. 21, 2019) (deciphering the "personality" of different fonts). MSC's website also uses "corporate blue," a color that is typically associated with business, "intelligence, stability, unity, and conservativism." *See* Jacci Howard Bear, *A Guide to the Color Corporate Blue*, LIFEWIRE (Dec. 20, 2018), https://www.lifewire.com/what-color-is-corporate-blue-1077385 [https://perma.cc/JQ39-X9WG] (explaining that people have certain feelings, emotions, and associations in response to typefaces and fonts).

220. *See GolfSuites 1*, *supra* note 210 (providing detailed information about the GolfSuites 1 investment opportunity).

221. *See Syndicates*, *supra* note 182 (defining a syndicate and showing users different options to begin investing with syndicates).

requirements,[222] with more than $1.8 trillion in capital raised via Regulation D in 2017.[223] While only 4% of this was via Reg D Rule 506(c),[224] that still accounts for $54 billion. Regulation A is a distant second, with about $500 million raised in 2017 via that exemption.[225] Regulation CF is another order of magnitude smaller in terms of offering volume with $59.2 million in proceeds reported in 2017.[226]

The table below summarizes the key differences among social media investment portals.

Portal Type	**Regulation**	**Investor Scrutiny**	**Financial Focus**	**Offering Volume**
Angel Investor	Reg D Rule 506(c)	High	Medium	High
Equity Crowdfunding	Reg CF	Low	Low	Low
Mini-IPO	Reg A	Medium	Medium	Medium

IV. "GENERAL SOLICITATION" ON SOCIAL MEDIA

Are social media investment portals engaged in "general solicitation"? Is all social media activity a "general solicitation" or is none of it? As discussed in Part II, general solicitation is a very important concept in securities law because certain exemptions to the requirement to register stock offerings with the SEC are only available where there has been "no general solicitation."[227] However, neither the SEC nor the courts have answered the question: What constitutes a general solicitation on social media? This part attempts to answer that question. Its analysis clarifies the value and necessity of portals. Moreover, this discussion sheds light on whether the general solicitation ban still makes sense in today's marketplace.

222. *See* Parnall, Kohl & Huff, *supra* note 128, at 634 (examining the history and evolution of Regulation D); *see also The Most Common Exemption –Regulation D Rule 506*, CAP. FUND L. BLOG, https://www.capitalfundlaw.com/blog/2015/04/05/the-most-common-exemptionregulation-d-rule-506 [https://perma.cc/5LKL-35FV] (last visited Sept. 2, 2020) (explaining Regulation D exemptions).

223. Ilirjan Pipa & Christopher Hawley, *SEC Reports Large Increase in Capital Raised via Private Placements*, MCDONALD HOPKINS (Nov. 15, 2018), https://mcdonaldhopkins.com/Insights/Blog/Business-Insights/2018/11/15/SEC-reports-large-increase-in-capital-raised-via-private-placements [https://perma.cc/JD7D-URRN].

224. *Id.*

225. Turner, *supra* note 164.

226. *2017 State of Regulation Crowdfunding Report*, CROWDFUND CAP. ADVISORS (Jan. 24, 2018), https://crowdfundcapitaladvisors.com/2017-state-regulation-crowdfunding-report/ [https://perma.cc/B85N-RTUL].

227. *Private Placements – Rule 506(b)*, SEC (Mar. 12, 2020), https://www.sec.gov/smallbusiness/exemptofferings/rule506b [https://perma.cc/U6Y2-V7Z2].

Although the SEC has not commented extensively on what actions are a "general solicitation," and has not commented on what social media actions would establish a violation of Regulation D, the SEC has provided some general guidance:

> "General solicitation" includes advertisements published in newspapers and magazines, public websites, communications broadcasted over television and radio, and seminars where attendees have been invited by general solicitation or general advertising. In addition, the use of an unrestricted, and therefore publicly available, website constitutes general solicitation. The solicitation must be an "offer" of securities, but solicitations that condition the market for an offering of securities may be considered to be offers.[228]

Aside from this general description, investors must rely on SEC no-action letters and the Compliance and Disclosure Interpretations (C&DIs) released by the SEC in 2013 to determine what could be a general solicitation. One characteristic that the SEC has emphasized repeatedly is the existence of a "pre-existing relationship" between the issuer and the potential investor. The SEC explained that a "pre-existing" relationship is "one that the issuer has formed with an offeree prior to the commencement of the securities offering or, alternatively, that was established through either a registered broker-dealer or investment adviser prior to the registered broker-dealer or investment adviser participation in the offering."[229] The existence of a pre-existing relationship is one means of demonstrating that an offering is not a general solicitation.

In some cases, it can be a challenge to determine when a pre-existing relationship has "commenced" for one investor but not for others. In an SEC no-action letter to Lamp Technologies, Inc., the Commission allowed solicitation through the use of a password-protected website.[230] Information about private offerings was allowed to be generally disseminated because the company required each investor to wait for a thirty-day period before they could participate in any offering.[231] This

228. *Eliminating the Prohibition Against General Solicitation and General Advertising in Rule 506 and Rule 144A Offerings*, SEC, sec.gov/info/smallbus/secg/general-solicitation-small-entity-compliance-guide.htm [https://perma.cc/A3GU-5P6L] (Sept. 20, 2013).

229. *Securities Act Rules Question 256.29: Compliance & Disclosure Regulations*, SEC, https://www.sec.gov/divisions/corpfin/guidance/securitiesactrules-interps.htm [https://perma.cc/65QH-DNQL] (Nov. 6, 2017) [hereinafter C&DI]; *see also* E.F. Hutton & Co., SEC No-Action Letter, 1985 WL 55680, at *1 (Dec. 3, 1985) (responding to request for interpretive advice regarding ensuring offerings did not involve general solicitations in violation of Rule 502(c)).

230. Lamp Technologies, Inc., SEC No-Action Letter No. 98-123, 2 (May 29, 1998) https://www.sec.gov/divisions/investment/noaction/1998/lamptech052998.pdf [https://perma.cc/WGT4-SLLX] [hereinafter Lamp Technologies].

231. *Id.* at 6.

further confuses the question of what constitutes a pre-existing relationship because it is not clear whether a thirty-day waiting period is a safe harbor, whether the particular facts of that situation made thirty days reasonable in that instance, or whether the SEC would ignore the result of this nonbinding nonaction letter in future matters altogether.

The *Lamp* holding also seems at odds with other SEC statements. In a no-action letter to *Citizen VC, Inc.*, the SEC recognized a pre-existing relationship because Citizen VC put investors through a vetting process that was "designed to evaluate the prospective investor's sophistication, financial circumstances and ability to understand the nature and risks of the securities to be offered."[232] It did not recognize a waiting period as a factor in evaluating the merits of *Citizen VC*.

The Commission has also concentrated on the specific type of information circulated to investors and the number of investors it has been circulated to in determining if general solicitation has occurred. As stated above, Rule 502(c), in addition to Rule 506(b), bans general solicitation. To avoid general solicitation, the SEC has stated that "factual business information that does not condition the public mind or arouse public interest in a securities offering is not an offer and may be disseminated widely" without contravening Rule 502(c).[233] "Factual business information . . . typically is limited to information about the issuer, its business, financial condition, products, services, or advertisement of such products or services, provided the information is not presented in such a manner as to constitute an offer of the issuer's securities."[234]

Even though the SEC has not placed a hard limit on the number of investors an issuer can communicate with, they have considered it a factor in determining if there has been general solicitation. "Further, any publication of information by a company in registration other than by means of a statutory prospectus should be limited to factual information and should not include such things as predictions, projections, forecasts or opinions with respect to value."[235] Additionally, the Commission noted, "the greater the number of persons without financial experience, sophistication or any prior personal or business relationship with the

232. Citizen VC, Inc. Response of the Office of Chief Counsel Division of Corporate, SEC No-Action Letter Finance (Aug. 6, 2015) https://www.sec.gov/divisions/corpfin/cf-noaction/2015/citizen-vc-inc-080615-502.htm [https://perma.cc/SHB8-AM5F].

233. C&DI, *supra* note 229, at Question 256.24.

234. *Id.* at Question 256.25.

235. Guidelines for Release of Information by Issuers Whose Securities are in Registration, 36 Fed. Reg. 16,506, 16,507 (Aug. 21, 1971).

issuer that are contacted . . . the more likely the communications are part of a general solicitation."[236]

Generally, publicly available information, if published, is not considered a general solicitation. In 1986, the SEC wrote they would not take action against Nancy Blasberg for publishing and selling a guide to investment banking firms that contained information such as name, address, phone number, date of issue, dividend rate, number of shares originally issued, and other things, as they pertained to outstanding privately-placed preferred stock issues.[237] The Commission commented that the guide only contained "certain limited information" on already "completed offerings."[238] This conclusion is consistent with the earlier letter to Richard Daniels which said it would not be a violation of the ban on general solicitation proscribed by Rule 502(c) if "a newsletter setting forth information derived totally from public records" was published.[239]

Issuers of securities are permitted to circulate written materials to offerees as long as they are not intended to influence investor decisions. Publicly available information in the Blasberg and Daniels letters did not have the effect of swaying the opinions of those to whom it was distributed. In 1986, J.D. Manning, Inc., asked the SEC if they could publish a newsletter that listed and described "closely held businesses" in southwest Florida "which may expect to raise capital in future transactions."[240] Businesses in the region would pay a fee for the right to have some of the information they provided to J.D. Manning selected for publication.[241] The SEC noted that although some of that information may have been factual in nature, it appeared "that an offer, within the purview of section 2(3) of the Securities Act," may be involved, so they could not "conclude that there would be no general solicitation for purposes of Rule 502(c)."[242]

All of this guidance, however, does not explicitly describe how it applies to the realm of social media. As of 2016, the average Facebook user had 155 "friends."[243] Does that constitute a pre-existing relationship

236. C&DI, *supra* note 229, at Question 256.27.
237. Nancy H. Blasberg, SEC No-Action Letter, 1986 WL 67060, at *1–2 (July 12, 1986).
238. *Id.* at *2.
239. Richard Daniels, SEC No-Action Letter, 1984 WL 45960, at *1 (Dec. 12, 1984).
240. J.D. Manning, Inc., SEC No-Action Letter, 1986 WL 65354, at *1 (Feb. 28, 1986).
241. *Id.* at *2.
242. *Id.* at *6.
243. *Facebook By the Numbers: Stats, Demographics & Fun Facts*, OMNICORE ANALYTICS, https://www.omnicoreagency.com/facebook-statistics/ [https://perma.cc/7ME7-E55N] (Apr. 22, 2020); Sarah Knapton, *Facebook Users Have 155 friends—But Would Trust Just Four in a Crisis*, TELEGRAPH UK (Jan. 20, 2016) https://www.telegraph.co.uk/news/science/science-news/12108412/Facebook-users-have-155-friends-but-would-trust-just-four-in-a-crisis.html [http://perma.cc/5HY4-UY48].

with all of them? Justin Tayler, a nightclub promoter, reached the 5,000 "friends" cap on Facebook.[244] Does that mean Mr. Tayler could solicit all of them for an investment opportunity? If a social network emerged that permitted a user to have tens of thousands or even millions of friends, would that constitute a pre-existing relationship with all of them? For that matter, former President Barack Obama has over 121 million followers on Twitter.[245] Does he have a pre-existing relationship with all of them? While these questions remain unresolved, companies and individuals like Karen should be reluctant to incur the SEC's attention by soliciting Facebook friends with investment opportunities.

Indeed, as that simple hypothetical illustrates, it may remain impossible to define what constitutes a pre-existing relationship on social media. The nature of relationships is different on each social media website. The degree to which this relationship has any relevance to securities offerings will also vary from network to network. On the one hand, networks formed for the purposes of sourcing investments would probably fall within the prohibition contemplated by *Citizen VC*. On the other hand, Facebook relationships may not. However, this is the inverse result of what a rational securities regulation should produce. Users who visit investment network sites are more likely to be sophisticated and able to protect themselves against fraudulent investment offerings than are users who are solicited while casually browsing on a social network site. Moreover, the lack of clarity makes all of this conduct risky.

Eliminating the ban on general solicitation would remove this issue. This is just one reason among many that the ban should be eliminated, but it is one that grows in weight as the nature of communication shifts more and more onto social networks. There are about 7.7 billion people in the world today, and 3.5 billion of them—nearly half—are online.[246] Facebook alone has 2.4 billion users.[247] Over 79% of all Americans are on social media as of 2019.[248] The number of social media users is predicted to continue to grow as internet adoption expands throughout

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244. Gabriel Rosu, *Meet the Guy with the Largest Number of Facebook Friends*, ETEKNIX (2015), https://www.eteknix.com/meet-guy-largest-number-facebook-friends/ [https://perma.cc/52ED-9As2].

245. *The Most Followed Accounts on Twitter*, BRANDWATCH (July 30, 2020) https://www.brandwatch.com/blog/most-twitter-followers/ [https://perma.cc/HA9L-SQVM].

246. Esteban Ortiz-Ospina, *The Rise of Social Media*, OUR WORLD IN DATA (Sep. 18, 2019), https://ourworldindata.org/rise-of-social-media [http://perma.cc/6ZVP-HCRV]

247. *Id.*

248. J. Clement, *Percentage of U.S. Population Who Currently Use Any Social Media from 2008 to 2019*, STATISTA (May 19, 2020) https://www.statista.com/statistics/273476/percentage-of-us-population-with-a-social-network-profile/ [https://perma.cc/D6CA-Y79A].

low-income countries[249] and rural communities in America.[250]

Curtis Jackson, more famously known as rapper 50 Cent, found himself backtracking to avoid trouble with the SEC in 2011 when he took to Twitter and urged his 3.8 million followers to buy stock in a company in which he was an investor.[251] He touted the ability to "double your money" if investors were to "get in now," and that the company was going to "blow[] up."[252] His actions sent the stock price "soaring some 270%."[253] Although the Commission never went after Jackson, it is likely because he quickly removed and replaced those tweets. Today, Jackson has over 12.1 million Twitter followers.[254]

Professional boxer Floyd Mayweather Jr. and music producer DJ Khaled were not as lucky as 50 Cent. In 2018, Mayweather tweeted that Centra Tech's ICO was about to start and urged his followers to buy by saying, "[g]et yours before they sell out, I got mine" while DJ Khaled described it on his Twitter as a "[g]ame changer."[255] Mayweather has over 7.8 million followers,[256] and DJ Khaled has over 5 million followers.[257]

Although it is clear that celebrities like Mayweather were openly trying to sway investor decision making, it seems untenable to determine that all of the other billions of users who are networked on various platforms have a pre-existing relationship sufficient to avoid the general solicitation

249. *See* Max Roser, Hannah Ritchie & Esteban Ortiz-Ospina, *Internet*, OUR WORLD IN DATA (2015), https://ourworldindata.org/internet#growth-of-the-internet [https://perma.cc/5DJ8-CZT7] (explaining that usage rates are increasing in the developing world).

250. *See* Lara Fishbane & Adie Tomer, *Broadband Adoption is on the Rise, but States Can Do Much More*, BROOKINGS (Oct. 10, 2019), https://www.brookings.edu/blog/the-avenue/2019/10/10/broadband-adoption-is-on-the-rise-but-states-can-do-much-more/ [https://perma.cc/8RSF-K3DL] (explaining that the digital divide between high adoption and low adoption states is narrowing and showing a correlation between larger rural populations and low adoptions rates).

251. Chris Barth, *Get Rich or Die Tweetin'*, FORBES (Jan. 11, 2011, 11:50 AM), https://www.forbes.com/sites/chrisbarth/2011/01/11/get-rich-or-die-tweetin/#5b7f71bf6df3 [https://perma.cc/5PYP-W7M6].

252. *Id*.

253. Kathy Kristof, *What 50 Cent Co. is Really Selling*, CBS NEWS (Jan. 18, 2011, 3:06 PM), https://www.cbsnews.com/news/what-50-cent-co-is-really-selling/ [https://perma.cc/Z3S7-VSX6].

254. 50cent (@50cent), TWITTER (2020), https://twitter.com/50cent?ref_src=twsrc^google|twcamp^serp|twgr^author [https://perma.cc/ZR9Y-4TXH].

255. *Press Release: Two Celebrities Charged with Unlawfully Touting Coin Offerings*, SEC (Nov. 29, 2018), https://www.sec.gov/news/press-release/2018-268 [https://perma.cc/GZX3-KQN7].

256. Floyd Mayweather (@FloydMayweather), TWITTER (2020), https://twitter.com/FloydMayweather?ref_src=twsrc^google|twcamp^serp|twgr^author [https://perma.cc/5QUW-JDQQ].

257. DJ Khaled (@djkhaled), TWITTER (2020), https://twitter.com/djkhaled?ref_src=twsrc^google|twcamp^serp|twgr^author [https://perma.cc/9EDF-QFFL].

ban. It goes without saying that some of the "friends" and "followers" shared between social media users must constitute pre-existing relationships; however, for the SEC, there is no clear way to distinguish between them. Yet the impossibility of applying the ban to social media at large is only one reason why it should be eliminated.

V. THE DEBATE ABOUT GENERAL SOLICITATION

Recall Karen, our small-town entrepreneur, and Kevin, the well-connected big-city businessman. It goes without saying that Kevin has access to more opportunities, among other advantages, due to his family, friends, and location. But in today's society, individuals are better connected than ever before. Indeed, "[t]he development of social networking sites (Facebook, Twitter, Instagram) in recent years, has radically changed both customers online purchasing habits and the way businesses promote their products and services."[258]

Sites like eBay connect buyers and sellers of used (and new) goods across states, spanning the country, and even the globe.[259] With the ability to connect buyers and sellers so efficiently, it seems reasonable that, as a society, we can provide the same ease of access to entrepreneurs and investors. Connecting people through the internet and social media should be just as easy. Karen can now have a level of access substantially closer to Kevin's.

It is not uncommon for regulation to lag behind innovation. We have seen a similar lag in other emerging markets, such as the ever-growing blockchain and cryptocurrency realm.[260] A similar lag has been seen with

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258. Curzi Valerio et al., *The Impact of Social Media on E-Commerce Decision Making Process*, 1 INT'L J. TECH. FOR BUS. (IJTB) 1, 1 (2019).

259. *See Selling Internationally*, EBAY, https://www.ebay.com/help/selling/selling/selling-internationally?id=4132 [https://perma.cc/QKX2-397W] (last visited Aug, 12, 2020) (providing users with information on how to sell internationally).

260. *See, e.g.*, Carla L. Reyes, *Moving Beyond Bitcoin to an Endogenous Theory of Decentralized Ledger Technology Regulation: An Initial Proposal*, 61 VILL. L. REV. 191, 193–95 (2016) ("This Article suggests a different approach . . . that both addresses potential market and government failures and takes into account the unique nature of the technology at issue."); Joshua A.T. Fairfield, *Bitproperty*, 88 S. CALIF. L. REV. 805, 869 (2015) ("There is a growing consensus that block chain technologies will be regulated."); Sarah Jane Hughes & Stephen T. Middlebrook, *Advancing A Framework for Regulating Cryptocurrency Payments Intermediaries*, 32 YALE J. REG. 495, 495 (2015) ("We use Article 4A of the Uniform Commercial Code as a model for regulating transactions in which intermediaries play a role."); Jeanne L. Schroeder, *Bitcoin and the Uniform Commercial Code*, 24 U. MIAMI BUS. L. REV. 1, 1 (2016) ("The bad news is [cryptocurrency] does not, and cannot be made to fit into, the U.C.C.'s definition of 'money'."); Michael Abramowicz, *Cryptocurrency-Based Law*, 58 ARIZ. L. REV. 359, 359 (2016) ("A modest starting point for cryptocurrency-based governance would be as a replacement for Bitcoin's centralized system for changing its source code.").

Uber, Lyft, and the gig economy,[261] as well as with advertising and data privacy.[262] As these examples illustrate, technological change frequently necessitates a change in law. Here, we see that a fundamental change in communication technology (social media) requires a change in the law regarding how we communicate about investment opportunities (general solicitation).

Many scholars have already commented on the need for regulatory change to the ban on general solicitation. Arguments have been advanced in favor of relaxing or completely removing the ban both in regard to ordinary as well as accredited investors. The primary argument for relaxing the ban is that the general solicitation ban was ill-conceived from the beginning. There is no legislative history that indicates why Congress instituted the ban in the first place. Over time, the federal anti-solicitation ban grew broader as judges sought to punish bad actors.[263] But, as is sometimes said, bad facts make bad law.[264] Along similar lines is the argument that the anti-solicitation ban was never needed because small offerings are too small to matter and large offerings go to purchasers who "do not really need Big Brother's protection."[265]

Another argument is that the thinking about how to regulate has dramatically changed since the securities regulations were first enacted in 1933. Even twenty years ago, scholars recognized that regulatory assumptions had changed over the sixty-five years since the securities regulations were enacted.[266] This resulted in sweeping changes to other regulations including privatizing fraud liability standards in unregistered offerings, validating party choice in domestic and international securities

261. *See* Seth C. Oranburg, *Unbundling Employment: Flexible Benefits for the Gig Economy*, 11 DREXEL L. REV. 1, 1 (2018) (arguing for the creation of new legal paradigms to govern the gig economy).

262. *See* Suzanne Vranica, *How Privacy Rules Will Affect the Ad Industry*, WALL ST. J. (June 17, 2019) ("[A] surge in privacy regulation around the globe has marketers, publishers and platforms scrambling to make sure they are compliant with new laws and pending regulations."); Om Mahida, *It's 2020 and We Still Have a Data Privacy Problem*, THE NEXT WEB (Jan. 25, 2020) https://thenextweb.com/podium/2020/01/25/its-2020-and-we-still-have-a-data-privacy-problem/ [https://perma.cc/N4N9-7D7K] ("Europe and California have introduced regulations to protect individual consumer data, . . . yet there is no federal law to protect the rights of the individual.").

263. Patrick Daugherty, *Rethinking the Ban on General Solicitation*, 38 EMORY L.J. 67, 134 (1989).

264. *See* N. Sec. Co. v. United States, 193 U.S. 197, 400 (1904) (Holmes, Jr., dissenting) ("Great cases like hard cases make bad law. For great cases are called great, not by reason of their real importance in shaping the law of the future, but because of some accident of immediate overwhelming interest which appeals to the feelings and distorts the judgment.").

265. Daugherty, *supra* note 263, at 134; *see generally* GEORGE ORWELL, 1984 (1949) (creating the character, "Big Brother," who is always watching, supposedly for the best interests of the people, and who has become symbolic of mass government surveillance and abuse of civil liberties).

266. Alan R. Palmiter, *Toward Disclosure Choice in Securities Offerings*, 1999 COLUM. BUS. L. REV. 1, 135 (1999).

transactions, and upholding disclosure disclaimers and other contractual waivers in securities fraud cases.[267] Congress implemented cost-benefit analyses for securities fraud class actions, and the SEC began permitting broad choice as to offering methods and disclosure levels.[268] This increased attention to policing specific fraud after the fact should correspond with a decreased focus on precluding broad general categories (such as the categorical ban on advertising) of fundraising activities.[269]

Yet another argument is that the world has changed, and whatever protection may have been afforded by the ban is no longer necessary. The distinction between "public" and "private" offerings has eroded in today's world,[270] making the artificial statutory distinction problematically outdated.[271] Meanwhile, investors have become more sophisticated and therefore are less in need of these protections.[272]

To these weights on the scale in favor of relaxing or eliminating the ban on general solicitation, this Article adds two more. First, the vagaries of what constitutes a "general solicitation" in the context of social media chills and prevents activities that may not be barred at all. Second, removing the ban would allow ordinary investors to organize into syndicates on social media, which would allow them to be more efficient and to protect themselves as a group.

Moreover, there are alternative ways to redress harms caused by bad actors who are fooling innocent people into purchasing the "wrong" securities. Anti-fraud laws such as section 10(b) of the Securities

267. *Id.*

268. *Id.*

269. Paul G. Mahoney, *Technology, Property Rights in Information, and Securities Regulation*, 75 WASH. UNIV. L.Q. 815, 847–48 (1997).

270. *See, e.g.*, Martin Enserink & Gilbert Chin, *The End of Privacy*, 347 SCI. 490, 491 (2015) ("Privacy as we have known it is ending, and we're only beginning to fathom the consequences.").

271. *See* William K. Sjostrom, Jr., *Relaxing the Ban: It's Time to Allow General Solicitation and Advertising in Exempt Offerings*, 32 FLA. ST. U.L. REV. 1, 50 (2004) ("This persistence is not the result of strong ideology, but is the result of a seventy-year-old statutory distinction between public offerings and private or limited offerings entrenched by overlapping federal and state securities regulations.").

272. Jeremy Derman, *Does the SEC Rule the Job Creation Roost? Squaring SEC Rulemaking with the JOBS Act's Relaxation of the Prohibition Against General Solicitation and Advertising*, 47 SUFFOLK U.L. REV. 139, 163 (2014) ("Nonetheless, what the JOBS Act does accomplish by 'relaxing the ban' is the removal of an archaic rule that has little place in today's sophisticated securities market—one vastly different from that of 1982, when Regulation D was first promulgated.").

Exchange Act of 1934[273] and plain old common law fraud[274] protections can be applied ex post to redress such harms and to discourage such behaviors.

CONCLUSION

It is time for the SEC's ban on general solicitation of securities to be swept into the dustbin of history. The ban never had a clearly articulated goal, and this Article has shown that it has clear harms. The disparate impact of the ban against rural, poor, or otherwise less well-connected entrepreneurs is cause enough for its termination. Proof of the problem is highlighted by contrast: securities exemptions that permit general solicitation are more egalitarian. Such an unjust law should not stand.

The ban should also be dispensed with for its lack of clarity in our social media age. Technological changes often necessitate change in law; here, the advent of social media and its widespread use as a primary mode of communication by an entire generation of people required this re-examination of the nearly hundred-year-old proscription. Upon review, the ban proves to be severely deficient and highly problematic in our digital age.

The ban's prophylactic ends can be served by better means. To the extent that it serves some countervailing goal such as protecting investors, there are more efficient tools, such as anti-fraud laws, that better serve those ends. Therefore, the SEC should eliminate the ban against general solicitation in order to further its mission of protecting investors while facilitating capital formation.

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273. As codified under 17 C.F.R. § 240.10b-5 (2019):

> "It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange, (a) To employ any device, scheme, or artifice to defraud, (b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or (c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security."

274. *See* RESTATEMENT (THIRD) OF TORTS: LIAB. FOR ECON. HARM § 9 (AM. LAW INST. 2020) ("One who fraudulently makes a material misrepresentation of fact, opinion, intention, or law, for the purpose of inducing another to act or refrain from acting, is subject to liability for economic loss caused by the other's justifiable reliance on the misrepresentation.").