



*State of North Carolina
Department of the Secretary of State*

ELAINE F. MARSHALL
SECRETARY OF STATE

ANN B. WALL
General Counsel

**About the Revised Proposed PACES Act (Crowdfunding) Rules (pp. 1-2)
and Summary of the Revised and Newly Proposed Rules (pp. 2-7)**

About the Revised Proposed PACES Act (Crowdfunding) Rules

This is a publication of both newly proposed rules and revisions to the rules that were previously published in February 2017 ("the February rules"). These proposed rules consist of:

- (1) An entirely new section of proposed rules resulting from the Department's review of public comments received regarding the February rules;
- (2) Revisions to the February rules that were made based upon both the Department's own review of the February rules and of public comments on those rules; and
- (3) Rules that the Department had planned to propose in a second round of 2017 rulemaking.

In 2016, the North Carolina General Assembly enacted the North Carolina PACES Act, S.L. 2016-103, that created the Invest NC Exemption under the North Carolina Securities Act, Chapter 78A of the General Statutes. The PACES Act specifically delegates responsibility for adopting rules to the Secretary of State ("the Department"). The PACES Act also requires that the Department coordinate its interpretation and administration of the new crowdfunding law with related federal law and regulations.

The PACES Act creates an exemption from registration for intrastate offerings under North Carolina securities laws. In addition, the PACES Act coordinates the state exemption with intrastate exemptions in federal securities laws.

The PACES Act allows smaller enterprises in North Carolina to access capital needed to initiate new business ventures or grow existing ones. The Act permits raising money through small contributions from a large number of North Carolina investors if certain requirements are met and followed (also known as crowdfunding).

In developing these proposed rules, the Department has balanced the protection of the investing public with the need for direction and flexibility for the issuers, registered dealers, and intrastate Internet funding portals. These rules are necessary and appropriate for the public interest of facilitating investment by North Carolina residents in North Carolina businesses.

The Department has, to the extent necessary, coordinated these rules with federal crowdfunding rules. However, the Department has proposed PACES Act rules that it believes are clearer and easier to comply with than the federal rules while providing robust investor protection. Because the PACES Act and the crowdfunding industry are new, the Department anticipates future amendments to its rules. In order to facilitate such amendments, the Department has proposed short rules addressing discrete topics rather than a single, long, federal-style combined regulation. The Department has also reserved a few rule numbers for use in the future (if needed).

The Department has sought to propose rules that will allow an issuer to take the steps necessary to begin a crowdfunding offering while providing both the Department and the investing public with necessary disclosures.

The Department is proposing a new section .2100, Rules For Local Public Offerings (LPOs). The section allows issuers to seek capital in an amount up to \$250,000 in a local community offering that permits the use of general solicitation and advertising, without requiring the use of the internet. This new capital raising strategy is consistent with the recently adopted federal rule (Rule 147A of the Securities Act of 1933) that has no restriction on Offers, provided certain conditions are met. This new federal Rule 147A will become effective on April 20, 2017. The Section .2100 rules address who may file an LPO, limitations on LPOs, what is required in order to file an LPO, and permissible actions in connection with the offer and sale of an LPO. Section .2100 is in the forefront among intrastate crowd funding regulations across the country because it is intended to be used in connection with new federal regulations. It is, therefore, time limited to permit the Department to assess whether it is effective from a business perspective and provides adequate investor protections. Unless the Department readopts the Section .2100 rules, no new LPOs will be permitted after April 1, 2020 and the Section will expire in 2021.

Summary of the Revised and Newly Proposed Rules

1. Summary of Revisions to the 18 NCAC 06A Section .2000 rules published in February 2017 and summary of newly proposed Section .2000 rules

18 NCAC 06A .2001, Purpose, and

18 NCAC 06A .2002, Scope: These rules clarify the purpose of, and scope of securities offerings under Section .2000.

18 NCAC 06A .2003, Definitions: Definitions of the following were added: blind pool, commodity pool, document, escrow account, escrow agent, lawyer, legal identity, minimum offering amount, target date, and target amount.

18 NCAC 06A .2004, Exemption Limitations: This is a newly proposed rule that clarifies requirements for the issuer to set a target date and amount as well as a minimum offering amount that is a percentage of the target amount. In addition to other limitations, the rule sets a 12 month outer limit for an offering relying on the exemption. The rule also bars reliance on the Exemption before the Administrator has reviewed the issuer's filings and issued a notice of compliance. An issuer is also prohibited from offering and selling securities without having filed with the Administrator and then trying to go back and file and rely on the Exemption.

18 NCAC 06A .2005, Counting Sales to Control Persons: The Act addresses sales to the issuer's control persons. The rule clarifies that those sales cannot be counted with regard to the issuer's minimum and target offering amounts.

18 NCAC 06A .2007, Initial Issuer Filing Requirements: This rule provides a general filing overview for issuers who seek to rely on the Exemption.

18 NCAC 06A .2008, Notice of Intrastate Claim of Exemption Form Requirements: Several types of businesses for which crowdfunding cannot be used have been added. An issuer will also have to provide additional information if the issuer is not using a funding portal or a registered dealer.

18 NCAC 06A .2009, Signing Form NCE: For corporations and nonprofit corporations, the revised proposed rule will allow the same people to sign the form as could sign a filing with the Secretary of State's Corporations Division.

18 NCAC 06A .2010, Content of Disclosure Document: The revised proposed rule adds disclosures to investors and the Administrator, including a description of the procedure investors must use to cancel an investment.

18 NCAC 06A .2011, Required Statements to Include in Issuer Disclosure Document: No substantive revisions have been made to the proposed rule.

18 NCAC 06A .2012, Circumstances When Additional Disclosure Document Content Required: The proposed rule has been revised to address the need for interim financial statements in some circumstances.

18 NCAC 06A .2013, Issuer to Cease Offering and Amend the Disclosure Document: No substantive revisions have been made to the proposed rule.

18 NCAC 06A .2014, Factors for Evaluation of the Form NCE, the Disclosure Documents, and the Claim of Exemption: This is a newly proposed rule addressing the factors the Administrator will consider when evaluating the Form NCE, Disclosure Document and Claim of Exemption.

18 NCAC 06A .2015, Administrator Notice of Compliance: This is a newly proposed rule that clarifies what will happen at the conclusion of the Administrator's evaluation of the Form NCE, Disclosure Document and Claim of Exemption.

18 NCAC 06A .2017, Escrow Account: This revised proposed rule clarifies the requirements for establishment of an escrow account and for an attorney serving as the escrow agent.

18 NCAC 06A .2018, Issuer to Provide Information to the Escrow Agent: No substantive revisions have been made to the proposed rule.

18 NCAC 06A .2019, Terms of Escrow Agreement: This revised proposed rule supplements the terms that must be included in the escrow agreement for the protection of not only the issuer and investor but also the escrow agent.

18 NCAC 06A .2020, Evaluation of the Escrow Agreement: This newly proposed rule addressing the factors the Administrator will consider when evaluating the Escrow Agreement.

18 NCAC 06A .2021, Administrator Escrow Agreement Approval, and 18 NCAC 06A .2022, Administrator Notice of Approval or Rejection of Escrow Agreement: These newly proposed rules clarify what will happen at the conclusion of the Administrator's evaluation of the Escrow Agreement.

18 NCAC 06A .2023, Escrow Agent Standards of Conduct: This newly proposed rule addresses escrow agent standards of conduct.

18 NCAC 06A .2024, Notice to Administrator of Funds Released from the Escrow Account, and 18 NCAC 06A .2025, Content of Notice of Release of Funds from Escrow Account: These two rules are a revision of a previously published rule and clarify who has to file the notice with the Administrator, when the notice must be filed and what information the notice must include.

18 NCAC 06A .2026, Registered Dealer Acting as an Escrow Agent, and 18 NCAC 06A .2027, Escrow Agent Requirements: These two rules revise a previously published rule and clarify the requirements for the escrow agent, including information the agent must obtain from the issuer or investors.

18 NCAC 06A .2028, Treatment of Information: This newly proposed rule clarifies the confidentiality of information received by the Administrator directly or indirectly from a bank or depository institution under the PACES Act.

18 NCAC 06A .2030, Funding Portal Registration, 18 NCAC 06A .2031, Contents of Form NCFP, and 18 NCAC 06A .2032, Required Funding Portal Attestations: These revised proposed rules clarify registration requirements, including funding portal responsibility for protecting confidential issuer and investor personal identifying information.

18 NCAC 06A .2033, Evaluation of the Funding Portal Registration, 18 NCAC 06A .2034, Administrator Denial of Funding Portal Registration, and 18 NCAC 06A .2035, Administrator Notice of Approval or Denial of a Funding Portal Registration: These newly proposed rules address the factors the Administrator will consider when evaluating the funding portal registration and clarify what will happen at the conclusion of the Administrator's evaluation of the registration.

18 NCAC 06A .2036, Funding Portal Notice to Administrator of Changes: This revised proposed rule clarifies when the portal must notify the Administrator of changes to information on the portal's Form NCFP, changes in its ownership and changes to the issuers whose offerings are posted on its website. It provides three options for providing issuer change information to the Administrator.

18 NCAC 06A .2037, Funding Portal Financial Interest in Issuer: This revised proposed rule clarifies information about the financial interest that must be disclosed to investors. It also states that such funding portal financial interests cannot be included in calculations of the minimum offering amount and target offering amount.

18 NCAC 06A .2038, Funding Portal Denial of Access: This revised proposed rule clarifies the requirements of the original proposed rule.

**18 NCAC 06A .2039, Funding Portal Standards of Conduct, and
18 NCAC 06A .2041, Limitations on General Solicitation and Advertising:** No substantive revisions have been made to these proposed rules.

18 NCAC 06A .2042, Media Coverage of a Securities Offering: The newly proposed rule clarifies the status of media coverage that the issuer has not paid for and has not solicited.

**18 NCAC 06A .2043, Mandatory Content Requirement in Permitted Advertising Notice
18 NCAC 06A .2044, Other Requirements for Permitted Advertising Notices:** These two rules clarify the previously proposed limits on advertising and when it is permitted.

**18 NCAC 06A .2045, Establishing a Platform,
18 NCAC 06A .2046, Individuals Not Subject to Dealer Registration,
18 NCAC 06A .2047, Retention Of Platform Communications,
18 NCAC 06A .2048, Administration of Platform Communication Channels, and
18 NCAC 06A .2049, Additional Communication Channel Requirements:** Collectively, these revisions to previously proposed rules clarify the requirements related to platforms, communication channels and the requirements for their use and for records preservation.

18 NCAC 06A .2051, Providing Disclosures to Prospective Investors: This revised proposed rule clarifies when the disclosures must be made to prospective investors.

18 NCAC 06A .2052, Manner of Providing Disclosure and Other Documents to a Prospective Investor or an Investor: This newly proposed rule states that disclosures and other documents may be provided either in paper or electronic format to prospective investors and investors. An “opt-out” opportunity must be provided with regard to electronic notices and disclosures.

18 NCAC 06A .2053, Issuer Shall Require Investor Actions: No substantive revisions have been made to this proposed rule.

**18 NCAC 06A .2054, Investor Cancellation of Investment Commitment,
18 NCAC 06A .2055, Release of Funds in Escrow Account, and
18 NCAC 06A .2056, Issuer Notice to Investors Target Amount Reached:** No substantive revisions have been made to these proposed rules.

18 NCAC 06A .2057, Quarterly Reports: This newly proposed rule clarifies when the first and last quarterly reports are due, and what must be included in the reports.

18 NCAC 06A .2058, Conclusion of the Offering: This newly proposed rule clarifies requirements related to the report due at the conclusion of the offering and what must be included in the report.

18 NCAC 06A .2060, Issuer Recordkeeping Requirements: This revision of a previously proposed rule clarifies which records must be kept by the issuer.

18 NCAC 06A .2061, Funding Portal Recordkeeping Requirements: This revised proposed rule clarifies that the records that must be kept by a funding portal include records related to escrow accounts and issuers that the portal rejects.

18 NCAC 06A .2062, Requirement for Retention of Original or Equivalent: This revised proposed rule clarifies that copies of original records may be retained, as long as all meta-data and similar information is retained as well.

18 NCAC 06A .2063, Protection of Investors Against Fraud and Other Misconduct: No substantive revisions have been made to this proposed rule.

18 NCAC 06A .2064, Integration: This newly proposed rule addresses integration of offerings pursuant to the Exemption with other securities offerings.

18 NCAC 06A .2065, Request for Waiver,

18 NCAC 06A .2066, Factors Administrator May Consider with Regard to Waiver Requests, and

18 NCAC 06A .2067, Administrator Notice of Approval or Denial of a Waiver: These newly proposed rules address the issues described in their titles.

18 NCAC 06A .2068, Signatures,

18 NCAC 06A .2069, Electronic Signature, and

18 NCAC 06A .2070, Signature Verifies Information is True: These newly proposed rules address signatures generally, as well as signatures on forms and documents other than the Form NCE.

18 NCAC 06A .2071, Filing with the Administrator,

18 NCAC 06A .2073, Filing Electronically,

18 NCAC 06A .2074, Amending a Document Filed with the Administrator,

18 NCAC 06A .2075, Abandonment or Withdrawal of Filing, and

18 NCAC 06A .2076, Calculation of Time: These four newly proposed rules and one previously proposed rule (.2074) address general filing and administrative requirements.

2. Summary of newly proposed Section .2100 rules: The rules in this proposed new section address local public offerings (LPOs) under \$250,000.

18 NCAC 06A .2101, Purpose, and

18 NCAC 06A .2102, Scope: These rules clarify the purpose of, and relationship between, securities offerings under Section .2000 and Section .2100.

18 NCAC 06A .2103, Definitions, and

18 NCAC 06A .2104, LPO Limitations: These rules set the boundaries within which an LPO must be operated.

18 NCAC 06A .2105, Mandatory Conference: This rule requires that an LPO issuer meet with the Secretary of State's Securities Division staff prior to filing for an LPO.

18 NCAC 06A .2106, Filing Form NCE: This rule sets out the additional requirements for an LPO filing a Form NCE, including providing its social media and website information.

18 NCAC 06A .2107, ESCROW PROVISIONS: This rule clarifies that the escrow provisions in Section .2000 apply to LPOs.

18 NCAC 06A .2108, Optional Use of Internet by an Issuer of an LPO: This rule clarifies that while an LPO does not have to be conducted using the Internet, the issuer may choose to use the Internet.

18 NCAC 06A .2109, General Solicitation and Advertising Filing Requirements, and 18 NCAC 06A .2110, Unacceptable General Solicitation and Advertising: These rules clarify the limits on advertising in connection with an LPO.

18 NCAC 06A .2111, Administrator Review of General Solicitation and Advertising Materials: This rule provides for review by the Administrator of LPO related advertising and what actions the Administrator may take with regard to the advertising.

18 NCAC 06A .2112, Recordkeeping Requirements: This rule clarifies requirements for issuer recordkeeping in addition to those in Section .2000.

18 NCAC 06A .2113, Prohibited LPO Issuer Businesses,

18 NCAC 06A .2114, Administrator May Approve Certain Other LPOS, and

18 NCAC 06A .2115, Evaluation Of The Issuer Business: These rules clarify that an LPO issuer is subject to the prohibited business requirements of Section .2000. In addition, there are other businesses in which an issuer may not engage and use the LPO type of securities offering. For businesses not listed but that have complex business structures, application may be made to the Administrator for permission to use an LPO according to these rules.

18 NCAC 06A .2116, Sunset Provision: This rule provides that because the LPO is a unique new form of offering, the LPO rules will expire in 2021 and that no new LPO offerings will be accepted after April 1, 2020. NOTE: It is, of course, possible that after review of the new LPOs and their impact on North Carolina businesses' ability to raise capital as well as the protection of investors, the Administrator may determine that the LPO rules should not expire or should be readopted.