

## General Information

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<b>Agency</b>	North Carolina Department of the Secretary of State
<b>Rule Title</b>	Sunset Provision
<b>Citation</b>	18 NCAC 06A .2120
<b>Proposed Action</b>	North Carolina Department of the Secretary of State proposes to amend the sunset provision by extending the provision by five years.
<b>Agency Contact</b>	Ann Wall, <a href="mailto:awall@sosnc.gov">awall@sosnc.gov</a> 919-814-5310
<b>Authority</b>	N.C.G.S. §78A-49(a) and N.C.G.S. §78A-17.1(f)
<b>Impact Summary</b>	State Government: Minimal impact expected Local Government: Minimal impact expected Federal Government: Minimal impact expected Private Sector: Minimal impact expected <b>Substantial Impact: No substantial impact expected</b>
<b>Necessity</b>	This action is necessary to extend the upcoming scheduled sunset provision within the rules of the state based Crowdfunding program or otherwise referred to as the “Local Public Offerings (“LPOs”)”. This is not a substantive or policy rule change of any kind.

## Summary

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Under authority of N.C.G.S. §78A-49(a), the NC SOS is charged with making, amending, and rescinding rules the NC SOS finds are necessary or appropriate in the public interest or for the protection of investors and clients. This summary and purpose for the proposed rule change and the justification is one of those appropriate times.

Crowdfunding is basically a way for typically smaller businesses to raise small amounts of money (investment) from a broad number of investors – hence the named concept, Crowdfunding.

As a result of significant support from the Governor, members of the Council of State, numerous Cabinet Agencies and near unanimous bipartisan support at the NC General Assembly, the Securities Division of the NC Secretary of State office in 2015 was statutorily directed to design and implement a state based Crowdfunding offering. This program, also known as a “Local Public Offering (LPO) was designed to assist small businesses in raising additional financial capital to support economic development. Depending on market conditions at the time, access to small business loans and other financial capital products from banks and other financial institutions can vary. There needs to be additional options for raising financial capital – especially for small businesses that don’t typically have the time, resources or expertise to participate in large investment offerings regulated by the federal and state government. As such,

following the passage of authorizing legislation, the Securities Division, in consultation with the Legislature, OSBM, and the private sector, developed a state-based Crowdfunding program and initiated appropriate rule-making.

Today, now five years later, the North Carolina Secretary of State is simply proposing to amend those existing rules to extend the scheduled sunsets. More specifically:

- (1) Extend the sunset provisions to accept new Form NCE – LPO or other filing related to a new local public offering (“LPO”) by five years and
- (2) Extend the expiration of the rules in Section .2100 by five years. See the Appendix for the text of the proposed rule amendment.

In review of the proposed extension of the sunset provisions, the NC SOS estimates a non-substantial economic impact for local, state, and federal government. Additionally, we estimate a non-substantial economic impact for the private sector. Again, in time, as the number of small business applications for crowdfunding expand, accessing capital, creating jobs and expanding the economy - there may be more of an impact.

### **Purpose and Description of the Rule Change**

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18 NCAC 06A .2100, “Rules For Local Public Offerings”, concerns LPOs and is designed to promote the overall economic health of North Carolina. The NC SOS is proposing to amend the LPO Sunset Provision, 18 NCAC 06A .2120, by extending the sunset date for (1) accepting any new Form NCE-LPO or other filing related to a new LPO through April 1, 2025, and (2) extending the sunset date for Section 2100 through April 1, 2026.

As stated previously, the overall purpose of the crowdfunding rules are to provide additional tools to small businesses for investment and raising financial capital. Depending on market conditions at the time a business is exploring options for access to capital, it may be less expensive for the small business to explore the state’s Crowdfunding program, rather than traditional small business lending options. Dozens of states across the country have enacted Crowdfunding laws in recent years. Most states, including North Carolina, have seen very limited numbers of small businesses applying for these Crowdfunding programs. Especially as banks and other financial institutions have expanded and more freely opened up small business loan opportunities. However over time, as the market for Crowdfunding investment grows and as more small businesses become aware of the program, a secondary purpose would be to create jobs and improve the overall economic health of North Carolina.

From a programmatic standpoint, North Carolina offers a two-tiered approach to crowdfunding:

- (1) The first path, the NC Paces Offering (“NCPO”), is similar to federal crowdfunding in that it allows for the solicitation of and communication directly with investors, but only through the internet. This “internet-only” crowdfunding option prohibits general solicitation and advertising.
- (2) The second path, LPOs, permits advertising and general solicitation of and communication with investors in person. The LPO rules seek to accomplish the objective of providing businesses with a flexible tool for capital formation, but also protect the investing public.

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As we approach the current sunset provision, the NC SOS is encouraged by the positive feedback from the public. The business community has expressed an interest in maintaining LPO option to meet their future capital formation needs. We are approaching the 3<sup>rd</sup> anniversary of the adoption of the LPO rules. During that time, there has been favorable economic conditions and a small market of crowdfunding issuers. There simply has not been enough time to evaluate the effectiveness of the LPO rules on the business community.

During the same review period, there were no enforcement actions taken against issuers in the crowdfunding space. This observation is limited due to the small number of crowdfunding issuers and the short observation period.

This rule amendment is designed to extend the time available for the Administrator to accept new Form NCE-LPO or other filing related to new LPOs as of the effective date of the rule amendment through April 1, 2025. The current 18 NCAC 06A.2120(a) of the Sunset Provision restricts the Administrator from accepting any new Form NCE-LPO or other filing related to a new LPO after April 1, 2020. There will be a period of time between April 2, 2020 and the effective date of this rule amendment where the NC SOS will be unable to accept new Form NCE-LPO or other filings related to new LPOs. From April 2, 2020 through the effective date of this rule amendment, the NC SOS will continue to engage with North Carolina businesses interested in the LPO process and provide assistance with pre-filing reviews.

The five-year extension of 18 NCAC 06A.2120(b) would allow the rules in section 2100 to remain effective until April 1, 2026 and continue to meet the needs of North Carolina businesses and investors. Extending the Sunset Provision rule for a five-year period would further the mission of the NC SOS of protecting North Carolina investors while promoting opportunities for North Carolinians to invest in local business.

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## **Estimated Impact**

### State Government

LPOs act as one of the capital formation offering options regulated by the NC SOS and available to businesses. The choice of capital formation offerings among the menu of regulated options has no significant impact on the workload of the NC SOS. The extension of the LPO rules does not create an increase in demand for capital formation, but instead provides another option for raising capital. NC SOS will not experience any additional workload for the processing of LPOs, as it is simply an alternative to NCPOs or the sale of securities. NC SOS's oversight of LPOs is a service that continues to fit within the agencies' current two-tiered approach and does not require additional budget resources. It also does not change the distribution or allocation of state funds.

If the Sunset Provision were to expire without an amendment, the NC SOS would continue to use its administrative resources to protect the investing public in the traditional areas of securities oversight. With the proposed amendment to extend the Sunset Provision for five

years, the NC SOS will continue to balance the protection of the investing public and the public's desires for choices in the area of capital formation. Since LPOs are not a program, an issuer choosing the LPO option for raising capital does not impact the NC SOS workload. Similarly, the amendment to extend the Sunset Provision extends the availability of the LPO option does not impact the workload of the NC SOS. The proposed Sunset Provision rule amendment does not have a substantial economic impact and will not require the expenditure or change the distribution of any State funds.

### Local Government

The proposed rule amendment will not affect local government or local government expenditures.

### Federal Government

The proposed rule amendment will not affect the federal government and no federal funds are required.

### Private Impact

The Sunset Provision amendment is necessary and appropriate for the public interest of facilitating opportunities for North Carolinians to invest in local businesses, while also protecting North Carolina investors. The proposed Sunset Provision amendment will continue to allow North Carolina businesses to continue to have the LPO path as a capital formation option.

If the Sunset Provision were to expire without an amendment, issuers wishing to pursue crowdfunding as a means for capital formation in North Carolina would only have the NCPO option available. As NCPO is the internet-only option, businesses using this path to crowdfunding would be unable to solicit friends and neighbors or advertise in their community. Since North Carolina has not yet had a NCPO issuer finish the process and release the escrow funds, it cannot be determine whether the absence of the LPO option would increase NCPO issuers. Similarly, at this time there is insufficient information to determine what alternative options to capital formation businesses may pursue if the LPO option has expired. Amending the Sunset Provision and extending its effectiveness for five-years, allows businesses to find investors in a greater number of ways as it allows solicitation and advertising. Since the adoption of the LPO rules, one LPO issuer successfully completed the LPO option and \$21,000 in escrow funds raised by the investors were released to the business for its improvements. The NC SOS is encouraged by this successful use of the LPO option, but requires additional time to determine the effects of the rules or the alternative capital formation options has on the success of LPOs.

The business community has expressed concern regarding the expirations contained in the current Sunset Provision and are hopeful a rule amendment will allow the LPO option to remain available in the future. The amendment to the Sunset Provision would allow the business community to continue to assess and choose the LPO option to meet their capital formation needs for an additional five years.

## APPENDIX

18 NCAC 06A .2120 is proposed for amendment as follows:

### **18 NCAC 06A .2120      SUNSET PROVISION**

- (a) The Administrator shall not accept any new Form NCE-LPO or other filing related to a new LPO after April 1, 2025.
- (b) The rules in this Section shall expire on April 1, 2026.

*History Note:*      *Authority G.S. 78A-17.1(a)(5); 78A-17.1(f); 78A-49(a); 78A-49(d); 78A-64; 78C-30; S.L. 2016-103, s.4.(a);*

*Eff. April 1, 2017 to expire on April 1, 2021.*

Amended Eff. July 1, 2020 to expire on April 1, 2026