

INSURANCE COVERAGE FOR CROWDFUNDING

On April 5, 2012, the Jumpstart Our Business Startups (JOBS) Act was signed into law by President Barack Obama. The stated purpose of the Act is to “increase American job creation and economic growth by improving access to the public capital markets for emerging growth companies.” On October 23, 2013, the SEC released proposed rules establishing a framework for crowdfunding offerings which have been regulated under the JOBS Act. The public comment period for the proposed rules ended on February 3, 2014. On April 10, 2014, the Investor Advisory Committee voted unanimously to ask the SEC to adopt a series of recommendations to the proposed crowdfunding rules.

While the term “crowdfunding” is not defined in the JOBS Act, it is commonly understood to mean the collective actions of people who pool their money and other resources together, usually via the internet, to support the efforts of others. Websites such as Kickstarter and IndieGoGo are popular examples of web-based crowdfunding sites.

Now, as the investing public awaits SEC guidance on crowdfunding regulations, the moment should not pass without acknowledging that the implementation of the rules may result in significant liability for issuers and intermediaries, as well as the directors and officers of such companies.

Insurance Issues associated with the SEC’s Crowdfunding Regulations

It has suggested that the JOBS Act will have the consequences of increasing IPOs, increasing private company financing flexibility, increasing securities litigation, and causing risk averse companies to elect to make more

complete disclosures.

These issues are expected to have insurance implications in a number of important ways. First, the traditional distinction between public and private companies in D&O policies will be blurred by the emergence of seemingly private companies, crowdfunded companies that are not publicly traded, yet exposed to more stringent disclosure requirements than a typical private company. Policyholders will therefore need to ensure that their insurance coverage covers their form of the company including any hybrid public-private company.

This is critical as some D&O policies for private companies contain exclusions pertaining to securities claims or “offerings”. Policyholders that may engage in crowdfunding activities will want to ensure that such activities are covered.

Second, policyholders will also want to ensure that the pertinent definition of “loss” covers losses which might arise out of crowdfunding. For example, some policies contain exclusions pertaining to disgorgement or, as aforementioned, securities claims. While policy language can vary widely, it is important for those engaged in crowdfunding to have coverage in the event of a suit by investors which could necessarily entail the reimbursement of invested capital.

Third, policyholders should closely analyze any fraud or dishonesty exclusions, if present in any pertinent policies, to ensure that the insurance company will not seek to bar coverage in the event that investors assert fraud claims in connection with crowdfunding. **ISN**



Source: Anderson Kill; Authored by Peter A. Halprin, Anderson Kill, New York