How to Choose Between US SEC Exemptions 504 and 506(b)

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Executive Summary

- Raising under $10 million? Rule 504 is the simplest option.
- Raising an unlimited amount? Rule 506(b) is your choice.
- Want to advertise publicly? Rule 504 may allow it (check state laws), but Rule 506(b) strictly forbids it.
- Selling to non-accredited investors? Rule 504 is more flexible, while 506(b) limits you to 35 "sophisticated" ones.
- Important for FlexUp Users: Issuing Credits or Tokens for an investment is likely a **securities offering** under U.S. law and requires compliance: registration – which is cumbersome – or exemption.

Overview

Under the U.S. Securities Act of 1933, any offer or sale of securities must be either:

- **Registered** with the U.S. Securities and Exchange Commission (SEC), or
- **Exempt** from registration under one of several specific rules.

For startups and early-stage projects, two common exemptions under **Regulation D** are:

- **Rule 504** — often referred to as the "seed capital" exemption
- **Rule 506(b)** — known as the "private placement" exemption

Choosing the right exemption is a strategic decision. It depends on how much you want to raise, from whom, and how you plan to reach those investors.

Rule 504 vs. Rule 506(b): Key Differences

The main differences lie in the **amount of money** you can raise, **who you can raise it from**, and **how you can advertise** the offering.

Feature	**Rule 504** (The "Seed Capital" Exemption)	**Rule 506(b)** (The "Private Placement" Exemption)
Offering Limit	Up to $10 million in a 12-month period*	No limit
Investor Type	Any number of accredited and non-accredited investors (state laws may vary)	Unlimited accredited investors + up to 35 non-accredited, sophisticated investors
Investor Sophistication	No federal requirement	Non-accredited investors must be "sophisticated" (able to evaluate the investment)
General Solicitation	Allowed only if the offering complies with specific state laws ("Blue Sky" laws) that	**Prohibited**. You cannot use general advertising (e.g., social media, public

	require disclosure documents and investor protections	websites, mass emails) to market the offering. You must have a pre-existing, substantive relationship with all investors.
Securities Status and Transfer Restrictions	Securities are "**restricted**" and cannot be freely resold unless registered under state law.	Securities are **always** "restricted" and resale requires registration or another exemption.

** This limit is subject to change; verify current regulations*

Summary: When to Choose Each

- **Rule 504** is well-suited for **smaller, early-stage raises**, especially if you want to **reach a broader investor base**, including the general public in certain states.
- **Rule 506(b)** is better for **larger, private placements**, where you're targeting **accredited investors** or a small group of sophisticated participants.

Who Qualifies as an Accredited Investor?

Defined under **Rule 501** of Regulation D, an *accredited investor* is a person or entity with the financial knowledge and resources to assume the risks of private investments.

Common Ways to Qualify (Individuals):

- **Income Test**:
  $200,000 annual income (individual) or $300,000 with spouse/partner for the last two years, with the expectation of the same this year.
- **Net Worth Test**:
  Net worth exceeding $1 million, excluding primary residence.
- **Professional Certification**:
  Holders of Series 7, 65, or 82 licenses in good standing.

Common Ways to Qualify (Entities):

- Banks, insurance companies, and registered investment companies.
- Trusts with assets exceeding $5 million.
- Entities owned entirely by accredited investors.

The purpose of these criteria is to **protect less experienced investors** from the higher risks associated with private, early-stage investments.

How Does This Relate to FlexUp?

FlexUp promotes a **flexible, transparent, and collaborative approach** to financing projects, with a focus on **fair risk-sharing** among all participants through:

- **Flexible remuneration** (base, flex, equity)
- **Deferred payments**
- **Tokens and credits as forms of equity**

Although FlexUp does **not itself issue securities**, projects using the FlexUp platform may raise funds under U.S. law and therefore must **comply with applicable exemptions** if they are offering investment opportunities to U.S. persons.

When a FlexUp Project Might Use Rule 504:

- Early-stage capital raise under $10 million
- Broader outreach needed (subject to state laws)
- Securities offered to non-accredited participants (e.g., clients, suppliers) as part of a broader ecosystem

When a FlexUp Project Might Use Rule 506(b):

- Larger or institutional fundraising
- Tight control over who is investing
- Strong preference for confidentiality and no public marketing

💡 Even under the FlexUp model, any issuance of profit-sharing rights (Credits or Tokens) in return for investment could be considered a securities offering under U.S. law. Projects are responsible for identifying the correct exemption and complying with it.

Note on FlexUp Charter Resale Restrictions

- In addition to legal restrictions imposed by U.S. securities law, resale and transfer of tokens issued under a FlexUp Charter are subject to restrictions defined in the project's Charter.
- These contractual limitations may require prior approval for transfers, restrict resale to approved parties, or limit the ability to trade such instruments on secondary markets.
- These rules are in place to ensure alignment with the project's purpose and governance structure, and they remain binding even when a U.S. securities exemption such as Rule 504 or 506(b) is used.
- These Charter-based restrictions operate in **addition** to the legal resale restrictions imposed under SEC regulations. Therefore, project owners and investors must ensure compliance with both the legal requirements of the SEC exemption and the contractual obligations of the FlexUp Charter.

Final Thoughts

Whether you are structuring an early-stage project or planning a large capital raise, it's essential to:

- Identify your investor base
- Understand your disclosure obligations
- Respect limits on solicitation
- Consider resale restrictions and investor expectations

Choosing the appropriate exemption can help ensure legal compliance and safeguard the long-term success of your project. FlexUp provides the tools and frameworks to help you manage your project's finances and equity transparently — but regulatory compliance remains your responsibility.

⚖️ **Remember: Always consult a securities attorney before offering investment opportunities in the U.S.**

(Information current as of Q3 2024. Please consult updated regulatory guidance before proceeding.)