EarlyShares

February 3, 2014

U.S. Securities and Exchange Commission
Attn: Elizabeth M. Murphy, Secretary
100 F Street NE
Washington, DC 20549-1090

Re: File No. S7-09-13 – Regulation Crowdfunding Rule Proposals

Dear Ms. Murphy:

Thank you for the opportunity to comment on the proposed rules and for your consideration of our policy recommendations. We appreciate the tremendous effort, deliberation and coordination that took place in order to create the proposed rules and we welcome the opportunity to lend our voice to the discussion.

EarlyShares is an online funding platform that connects business owners seeking capital with individual investors under exemptions provided for in the JOBS Act. As an advocate for and early participant in the equity crowdfunding industry, we are optimistic for the positive impact that Regulation Crowdfunding can have on the nation and our economy. We also understand the complexities facing the Commission in balancing the objectives and protections required for all participants - issuers, investors and intermediaries.

The Commission was granted some flexibility in creating the rules and we are pleased with your position on several provisions in the proposal.

We agree that an intermediary should be permitted to rely on the representations of a potential investor regarding annual income, net worth, and the amount of total investments made over the past 12 months across all platforms.

We also agree with the "greater of" clarification on income and net worth, and that an issuer should be able to rely on the efforts that an intermediary takes in order to determine that the aggregate amount of securities purchased by an investor will not cause the investor to exceed the investor limits.

In addition, we are pleased with the flexibility granting issuers permission to conduct concurrent 506(c) offerings with 4(a)(6) offerings. This ability will open additional opportunities to issuers who seek the benefits of both exemptions, and we expect that many issuers will conduct concurrent offerings.

Notwithstanding these positives, we are concerned that certain provisions in the proposed rules will make it difficult for issuers and investors to receive the full benefit that was intended from the exemption. We believe that our recommendations provide a balanced approach by reducing the proposed cost and complexity of Regulation Crowdfunding offerings, while still maintaining the extremely high levels of investor protection necessary for the market to flourish.

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Our comments center on a few key topics:

1) **Financial Disclosure and Ongoing Reporting Requirements** – The time and expense required to prepare and to comply with financial disclosures and ongoing reporting requirements should be reduced and commensurate with the capabilities of the issuers.

2) **Requirements on Intermediaries with Respect to Transactions: Issuer Information** – The requirement that all information about offerings be made publicly available should be balanced against an issuer's interest to protect sensitive and proprietary data. Issuers should be given control over who has access to sensitive and proprietary information.

3) **Safe Harbor for Certain Activities:**

    a) **Limiting Offerings** – Funding portals should be given broader discretion in their ability to limit offerings in order to differentiate themselves from one another and to disqualify certain issuers for a combination of objective and subjective reasons.

    b) **Highlighting Issuers and Offerings** – Issuers should have the ability to compensate funding portals to highlight their offerings on a funding platform as long as it is clear and prominently indicated that it is a "paid placement".

4) **Scope of Statutory Liability** – For the purpose of liability, funding portals should not be considered issuers. There are many other investor safeguards in place and this designation may create an insurmountable hurdle of accuracy and due diligence for funding portals who cannot reasonably verify every statement (or material omission) as it pertains to issuers on their platforms. The cost to comply, insure and/or defend against this liability is significant and misaligned with the role of a funding portal as we understand it.

In the following pages you will find a more detailed explanation as it relates to our points above.

1) Financial Disclosures and Ongoing Reporting Requirements

Proposed Rule 227.201(t) requires an issuer to provide financial information, reviewed or audited by a public accountant, depending on the offering size, at initiation of the offering and Proposed Rule 227.202 requires those disclosures to be provided on an ongoing annual basis.

Section 302(b)(1)(D) of the Act establishes tiered financial statement disclosure requirements that are based on aggregate target offering amounts within the preceding 12-month period. Section 302(b)(1)(D)(iii) of the Act expressly provides the SEC with authority to change the amount of the $500,000 threshold by rulemaking. The JOBS Act did not require any of these financial disclosures to be ongoing.

The Commission estimated the costs of complying with these obligations on pages 358-359 of the proposed rules. Below we have prepared a summary of those costs as well as a "Total Cost" that is estimated based on a 5-year average life of the investment. Upon review, we believe that the cost of complying with the financial reporting requirements will be detrimental to the success of Regulation Crowdfunding.

Costs to Raise Capital under Title III Crowdfunding - As Estimated By SEC

	Under $100,000		$100,000-$500,000		Over $500,000- $1,000,000	
	Low	High	Low	High	Low	High
Cost to Issue- Year 1						
Intermediary Comp	2,500	7,500	15,000	45,000	37,500	112,500
EDGAR/Form C/Form C-U	6,460	6,460	6,460	6,460	6,460	6,460
Form C-AR	4,000	4,000	4,000	4,000	4,000	4,000
Annual Review/ Audit	NA	NA	14,350	14,350	28,700	28,700
Total Cost to Raise in Year 1	**12,960**	**17,960**	**39,810**	**69,810**	**76,660**	**151,660**
Additional Costs- Per Year						
Form C-AR	4,000	4,000	4,000	4,000	4,000	4,000
Annual Review/ Audit	NA	NA	14,350	14,350	28,700	28,700
	4,000	4,000	18,350	18,350	32,700	32,700
Annual Costs for 5 years	**20,000**	**20,000**	**91,750**	**91,750**	**163,500**	**163,500**
Form C-TR at termination	**600**	**600**	**600**	**600**	**600**	**600**
Total Cost	**33,560**	**38,560**	**132,160**	**162,160**	**240,760**	**315,760**
% Costs- relative to size of offering amount						
25,000	134%	154%				
50,000	67%	77%				
99,000	34%	39%				
101,000			131%	161%		
250,000			53%	65%		
499,000			26%	32%		
501,000					48%	63%
750,000					32%	42%
1,000,000					24%	32%

Based on our market research, the estimated costs may be higher than stated above, and the average life may be longer than 5 years, further increasing the total costs, especially since the annual requirements are perpetual. Regardless, the costs as presented and estimated are revealing. Assuming a 5-year life of an investment, an issuer's cost to raise $25,000 would be between 134-154% of the offering amount; $250,000 would cost between 53-65%; $501,000 would cost between 48-63%; and $1,000,000 would cost between 24-32%.

By way of comparison, even after allocating these expenses over the estimated life of the investment, the total costs in many of these scenarios are higher than the cumulative cost of an equivalent sized loan per usury interest rate limits in all states, which are set at levels deemed appropriate to protect borrowers from excessive costs in accessing capital.

Given these high costs, we are concerned that the proposed rules would create an environment that fosters adverse selection. The issuers that elect to face the costs of raising capital under the exemption may do so only as a last resort or only do so in conjunction with a Rule 506(c) offering. This group of issuers will further be limited to those who are able to bear the expense to prepare their offering, without certainty that their target offering amount will be reached.

Additionally, and equally compelling, we believe that the combination of the expenses and the management time required to fulfill the annual reporting requirements may actually harm the investors that the requirements are intended to help. Most investors will be making investments with a primary objective of seeking a financial return. They will expect a management team to allocate its time and money to focus on driving the growth and success of the business, rather than spending precious resources on onerous and expensive compliance requirements that they do not necessarily want.

Recommendations: Considering that the financial disclosures and ongoing reporting requirements are a large driver of the expenses, and that the JOBS Act does not require reviewed or audited financials to be part of the annual reports, we recommend that:

i) The threshold for audited financials be raised to the maximum amount allowable under law, effectively limiting the requirement to only target offering amounts of $1,000,000. By comparison, Regulation A, an exemption from securities registration that also permits solicitation of the offering and investment by non-accredited investors, does *not* require audited financials to be provided;

ii) For all offering amounts, the annual reporting requirement be limited to internally generated reports including a written business update, summary of key metrics (established by and relevant to each business) and internally generated unaudited financial statements that are certified by the principal executive officer to be true and complete in all material respects;

iii) Unnecessary expenses and complexity be eliminated from the offering process wherever possible. For example, Form C-U is estimated to cost an issuer $400 per transaction. We do not believe that filing additional reports to the SEC at regular intervals during the funding process will add value, clarity or protection to investors, but will instead add unnecessary time and expense. Given how online platforms operate, the online offering will always have the most updated information regarding funding status. Form C-U should be eliminated for this reason;

iv) The Commission consider allowing companies to "test the waters" in a similar manner to that currently permitted under Regulation A in order to better manage the challenges associated with the upfront costs of an offering. Issuers can then choose to incur the full preparation expense only when they have more confidence in achieving a successful raise; and

v) The Commission permits cash accounting as opposed to requiring certain issuers to transition to accrual accounting. This will save time and money for issuers while still offering investors accurate financials. We support Sara Hanks of CrowdCheck, Inc. in her recommendation on this matter.

2) Requirements on Intermediaries with Respect to Transactions – Issuer Information

Proposed Rule 227.303(a) requires an intermediary to make any information provided by the issuer pursuant to Section 4A(b) available to the SEC and potential investors. Proposed Rule 227.303(a)(4) prohibits an intermediary from requiring a person to establish an account in order to access issuer information. We understand that information must be publicly available to avoid the exclusion of groups of potential investors. That same interest must be balanced against an issuer's need to protect sensitive and proprietary information. Issuers must be given the ability to disclose such information only to potential investors to whom they have granted access.

We understand that some of the requirements are imposed by the Act itself, but the Commission should define each requirement under Section 4A(b) with issuer privacy and security interests in mind. We have learned from Rule 506(c) offerings on our platform that issuers want to know and manage who is accessing their sensitive information. To support this requirement, EarlyShares presents a public and a private portion for each issuer's offering page on our platform. This has become standard practice on many platforms like EarlyShares, and we believe it will also be crucial to the success of Regulation Crowdfunding offerings.

The security, privacy and control features we give to our issuers have been critical for them to build trust and be comfortable in the online environment. The public portions contain an overview of the business and its team. The private portions contain details regarding intellectual property, detailed financial information, and other proprietary information. If we had not given issuers the ability to control access to their sensitive information, they would have posted significantly less information about their businesses, to the ultimate detriment of investors and perhaps to the success of their offerings.

Rather than requiring that all information be made public, issuers and investors would benefit from a permission-based system on the funding portal. This would allow for more sensitive information to be provided to an investor once the investor is granted access to the private portion of the offering by the issuer.

Recommendation: Clearly define the materials that must be provided in 4A(b) with a minimalist approach regarding the amount and extent of information necessary to be provided publicly. The rules should permit an issuer to provide a cursory description of its business to all potential investors, thus enabling the issuer to reserve access to sensitive information for potential investors with whom it wishes to share that information. This two-step process will be critical to ensure that investors will have access to sensitive information before making an investment and enables issuers to maintain control over that information.

3) Safe Harbor for Certain Activities

a) Limiting Offerings

Proposed Rule 227.402(b)(1) states that a funding portal may not deny access to an issuer based on the advisability of investing in the issuer or its offering. This rule limits a funding portal from selecting criteria that it may determine is important in assessing the various characteristics of any issuer. For example, a funding portal may want management experience to be included in the eligibility criteria. Measuring experience is sometimes objective, but often includes subjective elements.

Additionally, a funding portal may want to select businesses that have certain levels of "traction", which is defined differently and with varied metrics across industries. A funding portal may want to focus on issuers who are post-revenue or profitable, or focus on other metrics of performance. While this data can be objectively measured, it may also have some subjective components that will vary based on the issuer and may therefore be prohibited. We request clarity in this regard and contend that these selection criteria should be permissible.

In our view, as long as funding portals clearly communicate their selection criteria, objective and subjective elements should be permitted and do not connote investment advice. Rather, they simply set the minimum hurdle required for entry onto the platform.

Further, funding portals need broad discretion and authority to utilize a reasonable basis to disqualify issuers. The proposed limitation will expose the funding portal to greater risk of potential liability under Section 4A(c) of the Act. As described below in Section 4 of this comment letter, there needs to be balance between the accountability (potential liability) with flexibility (the breadth of ability to limit offerings) in the two rules.

Recommendation: Funding portals should be permitted to limit offerings on the basis of subjective factors so long as the funding portal discloses the criteria and that such selection does not constitute a recommendation regarding the advisability of any investment listed on the funding portal's website. These activities simply serve to establish the minimal acceptance criteria and do not connote investment advice.

b) Highlighting Issuers and Offerings

Proposed Rule 227.402(b)(2)(iii) prohibits a funding portal from receiving any special or additional compensation for highlighting issuers or offerings on its platform. This is harmful to the issuer as it could hinder their ability to gain traction for their offering simply due to poor natural search visibility on the platform.

Portals should be able to receive compensation, and issuers should have the ability to pay to promote their offerings for better placement on a funding portal. This is common practice across the web, and consumers are quite familiar with the concept of "paid placements". If it is clearly and prominently indicated that the issuer has paid for the premium placement, this should not be construed as investment advice and would not be confusing or misleading to potential investors.

Recommendation: Permit a funding portal to have the ability to receive additional compensation for highlighting issuers or offerings on its platform as long as there is clear and prominent indication that it is a "paid placement".

4) Scope of Statutory Liability

Section 4A(c)(3) of the Act defines, for the purposes of the liability provision of Section 4A, an issuer as including "any person who offers or sells the securities in such offering"[1]. By the SEC's interpretation, intermediaries, including funding portals, would be considered issuers based on the definition in this liability provision.[2] However, this interpretation is not specifically mandated by the JOBS Act.

EarlyShares is deeply committed to investor protection and has incorporated significant levels of education, due diligence, compliance, and fraud prevention into our business process for 506(c) offerings and fully intends to do the same with 4(a)(6) offerings. We absolutely believe that funding portals should be held to extremely high standards of conduct, transparency and fraud prevention.

With that in mind, we strongly disagree with the interpretation of classifying funding portals as issuers for the purposes of determining liability. In our view, this concept places a potentially insurmountable burden on all funding portals.

Based on several other safeguards in the proposed rules, compliant funding portals will already be operating with high levels of prudence, care and transparency. The literal interpretation of this liability indicates that portals would have to independently verify the material accuracy of all information that an issuer provides, and be held liable even for unintentional material misstatements and omissions by issuers.

The cost and the practicality of implementing such a standard are unwieldy and difficult to contemplate. Alternatively, the cost to insure against the potential liability that this will create will be prohibitive, and may significantly stifle the market development.

This liability is further misplaced when viewed alongside a funding portal's limited ability to limit offerings as described in Section 3(a) of this comment letter. These two provisions, when drafted against each other, need to balance accountability (potential liability) with flexibility (the breadth of ability to limit offerings). If a funding portal is to be considered as an issuer for liability purposes, then the portal should have broad and absolute discretion on which issuers to accept.

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[1] Proposed Rules at p.280.
[2] *Ibid.*

Recommendation: For the purpose of the liability provision, funding portals should not be considered issuers. Instead, funding portals should clearly disclose the specific process and due diligence that has occurred. In conjunction with funding portal education programs and other fraud preventions, this disclosure should provide sufficient investor protection without subjecting funding portals to insurmountable due diligence and liability hurdles.

We appreciate the opportunity to present our comments for consideration. EarlyShares is deeply committed to this market and will fully implement all rules, regulations and policies as determined and required by the Commission. Our goal is to assist and guide issuers and investors through an investment process that is transparent, compliant and beneficial to all participants.

Please feel free to contact me at EarlyShares if there is anything that we may do to assist the Commission and its staff with this rulemaking process.

Joanna Schwartz, CEO
EarlyShares.com, Inc.