SECURITIES AND EXCHANGE COMMISSION

17 CFR Parts 200, 227, 232, 239, 240 and 249

[RELEASE NOS. 33-9974; 34-76324; File No. S7-09-13]

RIN 3235-AL37

CROWDFUNDING

AGENCY: Securities and Exchange Commission.

ACTION: Final rule.

SUMMARY: The Securities and Exchange Commission is adopting new Regulation Crowdfunding under the Securities Act of 1933 and the Securities Exchange Act of 1934 to implement the requirements of Title III of the Jumpstart Our Business Startups Act. Regulation Crowdfunding prescribes rules governing the offer and sale of securities under new Section 4(a)(6) of the Securities Act of 1933. Regulation Crowdfunding also provides a framework for the regulation of registered funding portals and broker-dealers that issuers are required to use as intermediaries in the offer and sale of securities in reliance on Section 4(a)(6). In addition, Regulation Crowdfunding conditionally exempts securities sold pursuant to Section 4(a)(6) from the registration requirements of Section 12(g) of the Securities Exchange Act of 1934.

DATES: The final rules and forms are effective [insert date 180 days after publication in the Federal Register], except § 227.400, Form Funding Portal and the amendments to Form ID are effective January 29, 2016.

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I. INTRODUCTION

A. Background

Crowdfunding is a relatively new and evolving method of using the Internet to raise capital to support a wide range of ideas and ventures. An entity or individual raising funds through crowdfunding typically seeks small individual contributions from a large number of people. Individuals interested in the crowdfunding campaign – members of the "crowd" – may share information about the project, cause, idea or business with each other and use the information to decide whether to fund the campaign based on the collective "wisdom of the crowd."

The Jumpstart Our Business Startups Act (the "JOBS Act"),[1] enacted on April 5, 2012, establishes a regulatory structure for startups and small businesses to raise capital through securities offerings using the Internet through crowdfunding. The crowdfunding provisions of the JOBS Act were intended to help provide startups and small businesses with capital by making relatively low dollar offerings of securities, featuring relatively low dollar investments by the "crowd," less costly.[2] Congress included a number of provisions intended to protect investors who engage in these transactions,[3] including investment limits, required disclosures by issuers,

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[1] Pub. L. No. 112-106, 126 Stat. 306 (2012).

[2] *See, e.g.*, congressional statements regarding crowdfunding bills that were precursors to the JOBS Act: 157 CONG. REC. S8458-02 (daily ed. Dec. 8, 2011) (statement of Sen. Jeff Merkley) ("Low-dollar investments from ordinary Americans may help fill the void, providing a new avenue of funding to the small businesses that are the engine of job creation. The CROWDFUND Act would provide startup companies and other small businesses with a new way to raise capital from ordinary investors in a more transparent and regulated marketplace."); 157 CONG. REC. H7295-01 (daily ed. Nov. 3, 2011) (statement of Rep. Patrick McHenry) ("[H]igh net worth individuals can invest in businesses before the average family can. And that small business is limited on the amount of equity stakes they can provide investors and limited in the number of investors they can get. So, clearly, something has to be done to open these capital markets to the average investor[.]").

[3] *See, e.g.*, congressional statements regarding crowdfunding bills that were precursors to the JOBS Act: 158 CONG. REC. S1781 (daily ed. Mar. 19, 2012) (statement of Sen. Carl Levin) ("Our bill creates new opportunities for crowdfunding but establishes basic regulatory oversight, liability, and disclosure rules that

and a requirement to use regulated intermediaries. The provisions also permit Internet-based platforms to facilitate the offer and sale of securities in crowdfunding transactions without having to register with the Commission as brokers.

In the United States, crowdfunding generally has not involved the offer of a share in any financial returns or profits that the fundraiser may expect to generate from business activities financed through crowdfunding. Such a profit or revenue-sharing model – sometimes referred to as the "equity model" of crowdfunding – could trigger the application of the federal securities laws because it likely would involve the offer and sale of a security. Under the Securities Act of 1933 ("Securities Act"), the offer and sale of securities is required to be registered unless an exemption is available. Some observers have stated that registered offerings are not feasible for raising smaller amounts of capital, as is done in a typical crowdfunding transaction, because of the costs of conducting a registered offering and the resulting ongoing reporting obligations under the Securities Exchange Act of 1934 ("Exchange Act") that may arise as a result of the offering. Limitations under existing regulations, including purchaser qualification requirements for offering exemptions that permit general solicitation and general advertising, have made private placement exemptions generally unavailable for crowdfunding transactions, which are intended to involve a large number of investors[4] and not be limited to investors that meet specific qualifications.[5]

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will give investors the confidence to participate in this promising emerging source of money for growing companies.").

[4] In this release, "investors" includes investors and potential investors, as the context requires. *See* Rule 100(d) of Regulation Crowdfunding.

[5] *See Eliminating the Prohibition Against General Solicitation and General Advertising in Rule 506 and Rule 144A Offerings*, Release No. 33-9415 (July 10, 2013) [78 FR 44771 (July 24, 2013)] (adopting rules to implement Title II of the Jumpstart Our Business Startups Act) ("Rule 506(c) Adopting Release"). Title II of the JOBS Act directed the Commission to amend Rule 506 of Regulation D to permit general solicitation or general advertising in offerings made under Rule 506, provided that all purchasers of the securities are accredited investors. Accredited investors include natural persons who meet certain income or net worth thresholds. Although this rule facilitates the type of broad solicitation emblematic of crowdfunding,

Moreover, someone who operates a website to effect the purchase and sale of securities for the account of others generally would, under pre-existing regulations, be required to register with the Commission as a broker-dealer and comply with the laws and regulations applicable to broker-dealers.[6] A person that operates such a website only for the purchase of securities of startups and small businesses, however, may find it impractical in view of the limited nature of that person's activities and business to register as a broker-dealer and operate under the full set of regulatory obligations that apply to broker-dealers.

B. Title III of the JOBS Act

Title III of the JOBS Act ("Title III") added new Securities Act Section 4(a)(6),[7] which provides an exemption from the registration requirements of Securities Act Section 5[8] for certain crowdfunding transactions. To qualify for the exemption under Section 4(a)(6), crowdfunding transactions by an issuer (including all entities controlled by or under common control with the issuer) must meet specified requirements, including the following:

- the amount raised must not exceed $1 million in a 12-month period;
- individual investments in all crowdfunding issuers in a 12-month period are limited to:
    - the greater of $2,000 or 5 percent of annual income or net worth, if annual income or net worth of the investor is less than $100,000; and

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crowdfunding is premised on permitting sales of securities to any interested person, not just to investors who meet specific qualifications, such as accredited investors.

6 Exchange Act Section 15(a)(1) generally makes it unlawful for a broker or dealer to effect any transactions in, or induce the purchase or sale of, any security unless that broker or dealer is registered with the Commission pursuant to Exchange Act Section 15(b). 15 U.S.C. 78o(a). *See* discussion in Section II.D.2. Because brokers and dealers both register as broker-dealers (i.e., there is no separate "broker" or "dealer" registration under Exchange Act Section 15(b)), we use the term "broker-dealer" in this release.

7 15 U.S.C. 77d(a)(6).

8 15 U.S.C. 77e.

- 10 percent of annual income or net worth (not to exceed an amount sold of $100,000), if annual income or net worth of the investor is $100,000 or more; and

- transactions must be conducted through an intermediary that either is registered as a broker-dealer or is registered as a new type of entity called a "funding portal."

In addition, Title III:

- adds Securities Act Section 4A,[9] which requires, among other things, that issuers and intermediaries that facilitate transactions between issuers and investors in reliance on Section 4(a)(6) provide certain information to investors and potential investors, take other actions and provide notices and other information to the Commission;
- adds Exchange Act Section 3(h),[10] which requires the Commission to adopt rules to exempt, either conditionally or unconditionally, "funding portals" from having to register as a broker-dealer pursuant to Exchange Act Section 15(a)(1);[11]
- mandates that the Commission establish disqualification provisions under which an issuer would not be able to avail itself of the Section 4(a)(6) exemption if the issuer or an intermediary was subject to a disqualifying event; and
- adds Exchange Act Section 12(g)(6),[12] which requires the Commission to adopt rules to exempt from the registration requirements of Section 12(g),[13] either conditionally or unconditionally, securities acquired pursuant to an offering made in reliance on Section 4(a)(6).

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9 15 U.S.C. 77a.

10 15 U.S.C. 78c(h).

11 15 U.S.C. 78o(a)(1).

12 15 U.S.C. 78l(g)(6).

13 15 U.S.C. 78l(g).

On October 23, 2013, we proposed new rules and forms to implement Title III of the JOBS Act.[14] We received over 485 comment letters on the Proposing Release, including from professional and trade associations, investor organizations, law firms, investment companies and investment advisers, broker-dealers, potential funding portals, members of Congress, the Commission's Investor Advisory Committee,[15] state securities regulators, government agencies, potential issuers, accountants, individuals and other interested parties. We have reviewed and considered all of the comments that we received on the Proposing Release and on Title III of the JOBS Act.[16] In this release, we are adopting new rules and forms to implement Sections 4(a)(6) and 4A and Exchange Act Sections 3(h) and 12(g)(6). The rules are described in detail below.

II. FINAL RULES IMPLEMENTING REGULATION CROWDFUNDING

Regulation Crowdfunding, among other things, permits individuals to invest in securities-based crowdfunding transactions subject to certain thresholds, limits the amount of money an issuer can raise under the crowdfunding exemption, requires issuers to disclose certain information about their offers, and creates a regulatory framework for the intermediaries that facilitate the crowdfunding transactions. As an overview, under the final rules:

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[14] *See* Rel. No. 33-9470 (Oct. 23, 2013) [78 FR 66427 (Nov. 5, 2013)] (the "Proposing Release"), *available at*: http://www.sec.gov/rules/proposed/2013/33-9470.pdf.

[15] The SEC Investor Advisory Committee ("Investor Advisory Committee") was established in April 2012 pursuant to Section 911 of the Dodd-Frank Wall Street Reform and Consumer Protection Act [Pub. L. No. 111-203, sec. 911, 124 Stat. 1376, 1822 (July 21, 2010)] (the "Dodd-Frank Act") to advise the Commission on regulatory priorities, the regulation of securities products, trading strategies, fee structures, the effectiveness of disclosure, initiatives to protect investor interests and to promote investor confidence and the integrity of the securities marketplace. The Dodd-Frank Act authorizes the Investor Advisory Committee to submit findings and recommendations for review and consideration by the Commission.

[16] To facilitate public input on JOBS Act rulemaking before the issuance of rule proposals, the Commission invited members of the public to make their views known on various JOBS Act initiatives in advance of any rulemaking by submitting comment letters to the Commission's website at http://www.sec.gov/spotlight/jobsactcomments.shtml. The comment letters relating to Title III of the JOBS Act submitted in response to this invitation are located at http://www.sec.gov/comments/jobs-title-ii/jobs-title-iii.shtml.

- An issuer is permitted to raise a maximum aggregate amount of $1 million through crowdfunding offerings in a 12-month period;
- Individual investors, over the course of a 12-month period, are permitted to invest in the aggregate across all crowdfunding offerings up to:
    - If either their annual income or net worth is less than $100,000, then the greater of:
        - $2,000 or
        - 5 percent of the lesser of their annual income or net worth.
    - If both their annual income and net worth are equal to or more than $100,000, then 10 percent of the lesser of their annual income or net worth; and
- During the 12-month period, the aggregate amount of securities sold to an investor through all crowdfunding offerings may not exceed $100,000.

Certain companies are not eligible to use the Regulation Crowdfunding exemption. Ineligible companies include non-U.S. companies, companies that already are Exchange Act reporting companies, certain investment companies, companies that are disqualified under Regulation Crowdfunding's disqualification rules, companies that have failed to comply with the annual reporting requirements under Regulation Crowdfunding during the two years immediately preceding the filing of the offering statement, and companies that have no specific business plan or have indicated their business plan is to engage in a merger or acquisition with an unidentified company or companies.

Securities purchased in a crowdfunding transaction generally cannot be resold for a period of one year. Holders of these securities do not count toward the threshold that requires an issuer to register its securities with the Commission under Section 12(g) of the Exchange Act if the

issuer is current in its annual reporting obligation, retains the services of a registered transfer agent and has less than $25 million in assets.

Disclosure by Issuers. The final rules require issuers conducting an offering pursuant to Regulation Crowdfunding to file certain information with the Commission and provide this information to investors and the relevant intermediary facilitating the crowdfunding offering. Among other things, in its offering documents, the issuer is required to disclose:

- Information about officers and directors as well as owners of 20 percent or more of the issuer;
- A description of the issuer's business and the use of proceeds from the offering;
- The price to the public of the securities or the method for determining the price, the target offering amount, the deadline to reach the target offering amount, and whether the issuer will accept investments in excess of the target offering amount;
- Certain related-party transactions;
- A discussion of the issuer's financial condition; and
- Financial statements of the issuer that are, depending on the amount offered and sold during a 12-month period, accompanied by information from the issuer's tax returns, reviewed by an independent public accountant, or audited by an independent auditor. An issuer relying on these rules for the first time would be permitted to provide reviewed rather than audited financial statements, unless financial statements of the issuer are available that have been audited by an independent auditor.

Issuers are required to amend the offering document during the offering period to reflect material changes and provide updates on the issuer's progress toward reaching the target offering amount.

In addition, issuers relying on the Regulation Crowdfunding exemption are required to file an annual report with the Commission and provide it to investors.

Crowdfunding Platforms. One of the key investor protections of Title III of the JOBS Act is the requirement that Regulation Crowdfunding transactions take place through an SEC-registered intermediary, either a broker-dealer or a funding portal. Under Regulation Crowdfunding, offerings must be conducted exclusively through a platform operated by a registered broker or a funding portal, which is a new type of SEC registrant. The rules require these intermediaries to:

- Provide investors with educational materials;
- Take measures to reduce the risk of fraud;
- Make available information about the issuer and the offering;
- Provide communication channels to permit discussions about offerings on the platform; and
- Facilitate the offer and sale of crowdfunded securities.

The rules prohibit funding portals from:

- Offering investment advice or making recommendations;
- Soliciting purchases, sales or offers to buy securities offered or displayed on its platform;
- Compensating promoters and others for solicitations or based on the sale of securities; and
- Holding, possessing, or handling investor funds or securities.

The rules provide a safe harbor under which funding portals can engage in certain activities consistent with these restrictions.

The staff will undertake to study and submit a report to the Commission no later than three years following the effective date of Regulation Crowdfunding on the impact of the regulation on

capital formation and investor protection. The report will include, but not be limited to, a review of: (1) issuer and intermediary compliance; (2) issuer offering limits and investor investment limits; (3) incidence of fraud, investor losses, and compliance with investor aggregates; (4) intermediary fee and compensation structures; (5) measures intermediaries have taken to reduce the risk of fraud, including reliance on issuer and investor representations; (6) the concept of a centralized database of investor contributions; (7) intermediary policies and procedures; (8) intermediary recordkeeping practices; and (9) secondary market trading practices.

A. Crowdfunding Exemption

Section 4(a)(6) provides an exemption from the registration requirements of Securities Act Section 5 for certain crowdfunding transactions. To qualify for this exemption, crowdfunding transactions by an issuer must meet specified requirements, including limits on the dollar amount of the securities that may be sold by an issuer and the dollar amount that may be invested by an individual in a 12-month period. The crowdfunding transaction also must be conducted through a registered intermediary that complies with specified requirements.[17] Title III also provides limitations on who may rely on the exemption and establishes specific liability provisions for material misstatements or omissions in connection with Section 4(a)(6) exempt transactions. As discussed below, the rules we are adopting are designed to aid issuers, investors and intermediaries in complying with these various limitations and requirements.

[17] *See* Section II.C for a discussion of the intermediary requirements. *See also* Section II.D for a discussion of the additional funding portal requirements.

1. Limit on Capital Raised

a. Proposed Rules

The exemption from registration provided by Section 4(a)(6) is available to a U.S. issuer provided that "the aggregate amount sold to all investors by the issuer, including any amount sold in reliance on the exemption provided under [Section 4(a)(6)] during the 12-month period preceding the date of such transaction, is not more than $1,000,000." Under Securities Act Section 4A(h), the Commission is required to adjust the dollar amounts in Section 4(a)(6) "not less frequently than once every five years, by notice published in the Federal Register, to reflect any change in the Consumer Price Index for All Urban Consumers published by the Bureau of Labor Statistics."

Consistent with the statute, we proposed in Rule 100(a) of Regulation Crowdfunding to limit the aggregate amount sold to all investors by the issuer in reliance on the new exemption to $1 million during a 12-month period. Capital raised through other exempt transactions would not be counted in determining the aggregate amount sold in reliance on Section 4(a)(6).

We also provided guidance clarifying our view that offerings made in reliance on Section 4(a)(6) will not be integrated[18] with other exempt offerings made by the issuer, provided that each offering complies with the requirements of the applicable exemption that is being relied upon for the particular offering.

Under Section 4(a)(6), the amount of securities sold in reliance on Section 4(a)(6) by entities controlled by or under common control with the issuer must be aggregated with the

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[18] The integration doctrine seeks to prevent an issuer from improperly avoiding registration by artificially dividing a single offering into multiple offerings such that Securities Act exemptions would apply to multiple offerings that would not be available for the combined offering. *See, e.g.*, Final Rule: Nonpublic Offering Exemption, Release No. 33-4552 (Nov. 6, 1962).

amount to be sold by the issuer in the current offering to determine the aggregate amount sold in reliance on Section 4(a)(6) during the preceding 12-month period. Under the proposed rules, for purposes of determining whether an entity is "controlled by or under common control with" the issuer, an issuer would be required to consider whether it has "control" based on the definition in Securities Act Rule 405.[19] As proposed, the amount of securities sold in reliance on Section 4(a)(6) also would include securities sold by any predecessor of the issuer in reliance on Section 4(a)(6) during the preceding 12-month period.

b. Comments on the Proposed Rules

A few commenters supported a $1 million limit on capital raised by an issuer in reliance on Section 4(a)(6),[20] while many other commenters believed that the proposed $1 million limit was too low and, in some instances, recommended higher limits.[21] Several commenters urged that the $1 million limit be net of fees charged by the intermediary to host the offering on the intermediary's platform,[22] while other commenters generally opposed this idea.[23]

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19 *See* 17 CFR 230.405 ("The term control (including the terms controlling, controlled by and under common control with) means the possession, direct or indirect, of the power to direct or cause the direction of the management and policies of a person, whether through the ownership of voting securities, by contract, or otherwise."). Exchange Act Rule 12b-2 contains the same definition. *See* 17 CFR 240.12b-2.

20 *See, e.g.*, Leverage PR Letter; StartEngine Letter 1; StartEngine Letter 2; Wilson Letter.

21 *See, e.g.*, Advanced Hydro Letter; Bushroe Letter; Cole D. Letter; Concerned Capital Letter; Hamman Letter; Harrison Letter; Hillside Letter; Jazz Letter; Kickstarter Coaching Letter; McCulley Letter; McGladrey Letter; Meling Letter; Miami Nation Enterprises Letter; Multistate Tax Service Letter; Peers Letter; Pioneer Realty Letter; Public Startup Letter 2; Qizilbash Letter; Rosenthal O. Letter; Sarles Letter; SBM Letter; Taylor R. Letter; Taylor T. Letter; Wales Capital Letter 1; Wales Capital Letter 3; WealthForge Letter; Wear Letter; Wilhelm Letter; Winters Letter; Yudek Letter.

22 *See, e.g.*, Benjamin Letter; FundHub Letter 1; Hackers/Founders Letter; Joinvestor Letter; Odhner Letter; Omara Letter; Public Startup Letter 2; RFPIA Letter; RoC Letter; RocketHub Letter; Seed&Spark Letter; Thomas Letter 1; Wales Capital Letter 1; Whitaker Chalk Letter; Wilson Letter.

23 *See, e.g.*, Arctic Island Letter 4; ASSOB Letter; Commonwealth of Massachusetts Letter; MCS Letter; PeoplePowerFund Letter.

Commenters were divided on the proposed guidance that other exempt offerings should not be integrated when determining the amount sold during the preceding 12-month period for purposes of the $1 million limit, with some supporting this approach,[24] and others opposing it.[25]

c. Final Rules

We are adopting as proposed rules that limit to $1 million the aggregate amount that may be sold to all investors by the issuer in a 12-month period in reliance on the new exemption.[26] We continue to believe this approach is consistent with the statute and will provide for a meaningful addition to the existing capital formation options for smaller companies while maintaining important investor protections. Moreover, Regulation Crowdfunding is a novel method of raising capital for smaller companies, and we are concerned about expanding the offering limit of the exemption beyond the level specified in Section 4(a)(6) at the outset of the adoption of final rules. Some commenters suggested that the $1 million limit be net of fees charged by the intermediary to host the offering on the intermediary's platform,[27] which would be an indirect way of increasing the $1 million limit. We are concerned that expanding the offering limit in this way would

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24 *See, e.g.*, AngelList Letter; Arctic Island Letter 4; Campbell R. Letter; CFA Institute Letter; CFIRA Letter 11; EarlyShares Letter; EMKF Letter; Farnkoff Letter; Feinstein Letter; Growthfountain Letter; Hackers/Founders Letter; Heritage Letter; NSBA Letter; Parsont Letter; Perfect Circle Solutions Letter; Public Startup Letter 2; RoC Letter; RocketHub Letter; Wales Capital Letter 1; Wefunder Letter; Whitaker Chalk Letter; Wilson Letter.

25 *See, e.g.*, AFL-CIO Letter (not integrating other exempt offerings will make crowdfunding available to larger companies and "crowd out" smaller companies that lack other options for raising capital); AFR Letter; Brown J. Letter; Consumer Federation Letter (not integrating other exempt offerings will allow issuers to evade regulatory requirements); Fund Democracy Letter (not integrating other exempt offerings will give issuers an incentive to engage in advertising in concurrent private offerings to indirectly publicly advertise their crowdfunding offering); IAC Recommendation; MCS Letter; NASAA Letter.

26 *See* Rule 100(a)(1) of Regulation Crowdfunding. There is a technical change to the rule text ("offer and sell securities" is changed to "offer or sell securities") to clarify that an issuer does not have to complete a sale in order to rely on the Section 4(a)(6) exemption for an offering.

27 *See, e.g.*, Benjamin Letter; FundHub Letter 1; Hackers/Founders Letter; Joinvestor Letter; Odhner Letter; Omara Letter; Public Startup Letter 2; RFPIA Letter; RoC Letter; RocketHub Letter; Seed&Spark Letter; Thomas Letter 1; Wales Capital Letter 1; Whitaker Chalk Letter; Wilson Letter.

provide less certainty and could raise interpretive questions, which would make the exemption more costly for issuers to comply with. If a funding portal's fees are not known in advance, for example, this may create uncertainty for issuers about how much capital they would be able to raise. Therefore, we are adopting as proposed the limit on the aggregate amount sold.

Title III provides that the $1 million limit applies to the "aggregate amount sold to all investors by the issuer, including any amount sold in reliance on the exemption provided under [Section 4(a)(6)]." Securities Act Section 4A(g), however, provides that "[n]othing in the exemption shall be construed as preventing an issuer from raising capital through means other than [S]ection 4[(a)](6)." Considered together, these two provisions create statutory ambiguity because the first provision could be read to provide for the aggregation of amounts raised in all exempt transactions, even those that do not involve crowdfunding, while the second provision could be read to provide that nothing in the Section 4(a)(6) exemption should limit an issuer's capital raising through other methods. We believe that the overall intent of providing the exemption under Section 4(a)(6) was to provide an additional mechanism for capital raising for startup and small businesses and not to affect the amount an issuer could raise outside of that exemption. Thus, we believe that only the capital raised in reliance on the exemption provided by Section 4(a)(6) should be counted toward the limit. Capital raised through other means should not be counted in determining the aggregate amount sold in reliance on Section 4(a)(6). The opposite approach – requiring aggregation of amounts raised in any exempt transaction – would be inconsistent with the goal of alleviating the funding gap for startups and small businesses because, by electing crowdfunding, such issuers would be placing a cap on the amount of capital they could raise. An issuer that already sold $1 million in reliance on the exemption provided under Section 4(a)(6), for example, would be prevented from raising capital through other exempt methods and,

conversely, an issuer that sold $1 million through other exempt methods would be prevented from raising capital under Section 4(a)(6).

In determining the amount that may be sold in reliance on Section 4(a)(6), an issuer should aggregate amounts it sold (including amounts sold by entities controlled by, or under common control with, the issuer, as well as any amounts sold by any predecessor of the issuer) in reliance on Section 4(a)(6) during the 12-month period preceding the expected date of sale and the amount the issuer intends to raise in reliance on the exemption. An issuer should not include amounts sold in other exempt offerings during the preceding 12-month period.

Further, in light of Section 4A(g) and for the reasons discussed above, we continue to believe that an offering made in reliance on Section 4(a)(6) should not be integrated with another exempt offering made by the issuer, provided that each offering complies with the requirements of the applicable exemption that is being relied upon for the particular offering. For example, an issuer conducting a concurrent exempt offering for which general solicitation is not permitted will need to be satisfied that purchasers in that offering were not solicited by means of the offering made in reliance on Section 4(a)(6).[28] As another example, an issuer conducting a concurrent exempt offering for which general solicitation is permitted, for example, under Securities Act Rule 506(c), could not include in any such general solicitation an advertisement of the terms of an offering made in reliance on Section 4(a)(6), unless that advertisement otherwise complied with Section 4(a)(6) and the final rules. As such, a concurrent offering would be bound by the more restrictive solicitation requirements of Regulation Crowdfunding, unless the issuer can conclude

[28] For a concurrent offering under Rule 506(b), an issuer will have to conclude that purchasers in the Rule 506(b) offering were not solicited by means of the offering made in reliance on Section 4(a)(6). For example, the issuer may have had a preexisting substantive relationship with such purchasers. Otherwise, the solicitation conducted in connection with the crowdfunding offering may preclude reliance on Rule 506(b). *See also* Rel. No. 33-8828 (Aug. 3, 2007) [72 FR 45116].

that the purchasers in the Regulation Crowdfunding offering were not solicited by means of the offering made in reliance on Rule 506(c).

The amount of securities sold in reliance on Section 4(a)(6) by entities controlled by or under common control with the issuer must be aggregated with the amount to be sold by the issuer in the current offering to determine the aggregate amount sold in reliance on Section 4(a)(6) during the preceding 12-month period. The statute does not define the term "controlled by or under common control with" the issuer; however, the term "control" is defined in Securities Act Rule 405.[29] Under the final rules, for purposes of determining whether an entity is "controlled by or under common control with" the issuer, an issuer will be required to consider whether it possesses, directly or indirectly, the power to direct or cause the direction of the management and policies of the entity, whether through the ownership of voting securities, by contract or otherwise, consistent with the definition of "control" in Securities Act Rule 405.[30]

Under the final rules, the amount of securities sold in reliance on Section 4(a)(6) also includes securities sold by any predecessor of the issuer in reliance on Section 4(a)(6) during the preceding 12-month period.[31] We believe this approach is necessary to prevent an issuer from exceeding the $1 million limit by reorganizing into a new entity that would otherwise not be limited by previous sales made by its predecessor.

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29 *See* note 19.

30 *See* Instruction to paragraph (c) of Rule 100 of Regulation Crowdfunding.

31 *See* Rule 100(c) of Regulation Crowdfunding (defining issuer, in certain circumstances, to include all entities controlled by or under common control with the issuer and any predecessor of the issuer).

2. Investment Limits

a. Proposed Rules

Under the exemption from registration set forth in Securities Act Section 4(a)(6)(B), the aggregate amount of securities sold to any investor by an issuer, including any amount sold in reliance on the exemption during the 12-month period preceding the date of such transaction, cannot exceed: "(i) the greater of $2,000 or 5 percent of the annual income or net worth of such investor, as applicable, if either the annual income or the net worth of the investor is less than $100,000; and (ii) 10 percent of the annual income or net worth of such investor, as applicable, not to exceed a maximum aggregate amount sold of $100,000, if either the annual income or net worth of the investor is equal to or more than $100,000."

In the Proposing Release, we noted that this statutory language may present ambiguity in some cases about which of the two investment limits governs, because paragraph (i) applies if "either" annual income or net worth is less than $100,000 and paragraph (ii) applies if "either" annual income or net worth is equal to or more than $100,000. Accordingly, in a situation in which annual income is less than $100,000 and net worth is equal to or more than $100,000 (or vice versa), the language of the statute may be read to cause both paragraphs to apply. Paragraph (i) also fixes the maximum annual investment by an investor at 5 percent of "the annual income or net worth of such investor, as applicable" and paragraph (ii) fixes the maximum annual investment by an investor at 10 percent of "the annual income or net worth of such investor, as applicable," but neither states when that percentage should be applied against the investor's annual income and when it should be applied against the investor's net worth.

Under proposed Rule 100(a) of Regulation Crowdfunding, the aggregate amount of securities sold to any investor by any issuer in reliance on Section 4(a)(6) during the 12-month

period preceding the date of such transaction, including the securities sold to such investor in such transaction, could not exceed the greater of: (i) $2,000 or 5 percent of the annual income or net worth of the investor, whichever is greater, if both annual income and net worth are less than $100,000; or (ii) 10 percent of the annual income or net worth of the investor, whichever is greater, not to exceed an amount sold of $100,000, if either annual income or net worth is equal to or more than $100,000.

We did not propose to alter these investment limits for any particular type of investor or create a different exemption based on different investment limits. Under the proposal, the annual income and net worth of a natural person would be calculated in accordance with the Commission's rules for the calculation of annual income and net worth of an accredited investor, and an investor's annual income or net worth could be calculated jointly with the annual income or net worth of the investor's spouse. An issuer would be able to rely on the efforts of an intermediary to determine that the aggregate amount of securities purchased by an investor will not cause the investor to exceed the investment limits, provided the issuer does not have knowledge to the contrary.

b. Comments on the Proposed Rules

Commenters were divided on the proposed investment limits. Many commenters supported some type of investment limit without necessarily expressing a specific opinion on the

proposed investment limits,[32] while many others generally opposed any type of investment limit.[33] A number of commenters recommended changes to the proposed limits.[34]

While some commenters supported the proposal to apply the higher investment limit (10 percent, as set forth in Section 4(a)(6)(B)(ii)) if only one of the annual income or net worth of the investor is equal to or more than $100,000,[35] some commenters also supported the lower investment limit ($2,000 or 5 percent, as set forth in Section 4(a)(6)(B)(i)) unless both the annual income and net worth of the investor are equal to or more than $100,000.[36]

A number of commenters supported the proposal that within each of the two levels of investment limits, the limits would be calculated based on the "greater of" an investor's annual income or net worth,[37] while a number of other commenters preferred a "lesser of" approach.[38] A few commenters suggested a combination of the approaches (*e.g.*, if either annual income or net worth is below $100,000, the lower investment limit level ($2,000 or 5 percent) would apply, but within that level, the limit would be based on the greater of annual income or net worth).[39]

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32 *See, e.g.*, Accredify Letter; Ahmad Letter; Crowley Letter; Farnkoff Letter; Merkley Letter; Milken Institute Letter; Patel Letter; Saunders Letter; StartEngine Letter 1; Wales Capital Letter 1.

33 *See, e.g.*, ASSOB Letter; Crowdstockz Letter; Hamman Letter; Holland Letter; McCulley Letter; Meling Letter; Qizilbash Letter; Ramsey Letter; SBM Letter; Taylor R Letter.

34 *See, e.g.*, Crowdstockz Letter; Gill Letter; Johnston Letter; Morse Letter; Qizilbash Letter; Vossberg Letter; Winters Letter.

35 *See, e.g.*, ABA Letter; CFA Institute Letter; CFIRA Letter 12; Craw Letter; Finkelstein Letter; RocketHub Letter; Wilson Letter.

36 *See, e.g.*, AFL-CIO Letter; BetterInvesting Letter; Consumer Federation Letter; Fund Democracy Letter; IAC Recommendation; Jacobson Letter; NASAA Letter; Schwartz Letter.

37 *See, e.g.*, ABA Letter; Anonymous Letter 6; CFIRA Letter 12; Craw Letter; EarlyShares Letter; Jacobson Letter; Omara Letter; RocketHub Letter; Wilson Letter.

38 *See, e.g.*, AFR Letter; BetterInvesting Letter; Consumer Federation Letter; Fund Democracy Letter; Fryer Letter; Growthfountain Letter; IAC Recommendation (stating that the "greater of" approach would be appropriate for accredited investors); Merkley Letter; NASAA Letter; Schwartz Letter; Zhang Letter (recommending that net worth not be used to calculate the investment limit).

39 *See, e.g.*, Consumer Federation Letter; Fund Democracy Letter; Jacobson Letter.

Many commenters supported the proposal that an issuer may rely on the efforts of an intermediary to determine that the aggregate amount of securities purchased by an investor will not cause the investor to exceed the investment limits, provided that the issuer does not have knowledge that the investor had exceeded, or would exceed, the investment limits as a result of purchasing securities in the issuer's offering.[40] A few commenters recommended that an issuer be required to obtain a written representation from the investor that the investor has not and will not exceed the limits by purchasing from the issuer.[41]

Commenters were divided about the joint calculation of annual income and net worth with the investor's spouse. Several commenters supported the proposal that an investor's annual income and net worth be calculated jointly with that of the investor's spouse,[42] while other commenters generally opposed that aspect of the proposal.[43] Several commenters recommended that if an investor's annual income and net worth are to be calculated jointly, the Commission should establish higher thresholds or an aggregate investment limit applicable to both spouses.[44]

A number of commenters favored different or no investment limits for accredited and institutional investors. Many commenters supported exempting accredited and institutional

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40 *See, e.g.*, Arctic Island Letter 4; CFA Institute Letter; Consumer Federation Letter; CrowdBouncer Letter; EarlyShares Letter; EMKF Letter; Finkelstein Letter; Fund Democracy Letter; Heritage Letter; Joinvestor Letter; Public Startup Letter 2; RoC Letter; RocketHub Letter; Vann Letter; Wefunder Letter; Whitaker Chalk Letter.

41 *See, e.g.*, FundHub Letter 1; Public Startup Letter 2; RocketHub Letter.

42 *See, e.g.*, Arctic Island Letter 4; Heritage Letter; Joinvestor Letter; NSBA Letter; Omara Letter; RocketHub Letter; Wilson Letter.

43 *See, e.g.*, Brown J. Letter; Consumer Federation Letter; Fund Democracy Letter; Jacobson Letter; Projectheureka Letter; Public Startup Letter 2.

44 *See, e.g.*, Brown, J. Letter; Consumer Federation Letter; Fund Democracy Letter; Jacobson Letter.

investors from the investment limits,[45] although a number of other commenters opposed such an exemption.[46] A few commenters recommended allowing higher investment limits for accredited and institutional investors.[47] One commenter stated that applying the investment limits to accredited and institutional investors would deter those investors from participating, but noted that allowing concurrent offerings under Securities Act Rule 506(c)[48] may mitigate this problem.[49]

c. Final Rules

Consistent with the statute, we are adopting investment limits for securities-based crowdfunding transactions, but with some modifications from the proposed rules. We have modified the final rules from the proposal to clarify that the investment limit reflects the aggregate amount an investor may invest in all offerings under Section 4(a)(6) in a 12-month period across all issuers. In addition, as noted above, some commenters supported a "greater of" approach to implementing the two statutory investment limits, while others supported a "lesser of" approach. After considering the comments received, we have decided to adopt a "lesser of" approach. Thus, under the final rules, an investor will be limited to investing: (1) the greater of: $2,000 or 5 percent of the lesser of the investor's annual income or net worth if either annual income or net worth is less than $100,000; or (2) 10 percent of the lesser of the investor's annual income or net

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45 *See, e.g.*, ASSOB Letter; Crowdstockz Letter; Crowley Letter; EMKF Letter; FundHub Letter 1; Gibb Letter; Heritage Letter; Joinvestor Letter; Public Startup Letter 2; RoC Letter; RocketHub Letter; Vann Letter; Wales Capital Letter 1; WealthForge Letter; Wefunder Letter.

46 *See, e.g.*, CFA Institute Letter; FundDemocracy Letter; Hackers/Founders Letter; Jacobson Letter; PeoplePowerFund Letter; Projectheureka Letter; Whitaker Chalk Letter; Wilson Letter.

47 *See, e.g.*, Growthfountain Letter; RFPIA Letter; WealthForge Letter.

48 17 CFR §230.506.

49 *See* Arctic Island Letter 4.

worth, not to exceed an amount sold of $100,000, if both annual income and net worth are $100,000 or more.[50]

Under this approach, an investor with annual income of $50,000 a year and $105,000 in net worth would be subject to an investment limit of $2,500, in contrast to the proposed rules in which that same investor would have been eligible for an investment limit of $10,500.[51] We recognize that this change from the proposed rules could place constraints on capital formation. Nevertheless, we believe that the investment limits in the final rules appropriately take into consideration the need to give issuers access to capital while minimizing an investor's exposure to risk in a crowdfunding transaction.

The chart below illustrates a few examples:

Investor Annual Income	Investor Net Worth	Calculation	Investment Limit[52]
$30,000	$105,000	Greater of $2,000 or 5% of $30,000 ($1,500)	$2,000
$150,000	$80,000	Greater of $2,000 or 5% of $80,000 ($4,000)	$4,000
$150,000	$100,000	10% of $100,000 ($10,000)	$10,000
$200,000	$900,000	10% of $200,000 ($20,000)	$20,000
$1,200,000	$2,000,000	10% of $1,200,000 ($120,000), subject to $100,000 cap	$100,000

A number of commenters expressed concerns about investors potentially incurring unaffordable losses under the proposed rule,[53] and we find these comments persuasive given the

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50 *See* paragraph (a)(2) of Rule 100 of Regulation Crowdfunding.

51 *See* Instruction 2 to paragraph (a)(2) of Rule 100 of Regulation Crowdfunding.

52 This "Investment Limit" column reflects the aggregate investment limit across all offerings under Section 4(a)(6) within a 12-month period.

53 *See, e.g.*, AFL-CIO Letter; BetterInvesting Letter; Consumer Federation Letter; Fund Democracy Letter; IAC Recommendation; Jacobson Letter; Merkley Letter; NASAA Letter; Schwartz Letter.

risks involved. The startups and small businesses that we expect will rely on the crowdfunding exemption are likely to experience a higher failure rate than more seasoned companies.[54] Applying the lower limit ($2,000 or 5%, rather than 10%) for investors whose annual income or net worth is below $100,000 and applying that formula to the lesser of annual income or net worth will potentially limit investment losses in crowdfunding offerings for investors who may be less able to bear the risk of loss. We are concerned about the number of households where there is a sizeable gap between net worth and annual income, and the ability of these households to withstand the risk of loss. According to Commission staff analysis of the data in the 2013 Survey of Consumer Finances, approximately 20% of U.S. households with net worth over $100,000 have annual income under $50,000.

Consistent with the proposed rules, the final rules allow an issuer to rely on efforts that an intermediary is required to undertake in order to determine that the aggregate amount of securities purchased by an investor does not cause the investor to exceed the investment limits, provided that the issuer does not have knowledge that the investor had exceeded, or would exceed, the investment limits as a result of purchasing securities in the issuer's offering.[55]

We are adopting, as proposed, final rules that allow an investor's annual income and net worth to be calculated as those values are calculated for purposes of determining accredited investor status.[56] Securities Act Rule 501 specifies the manner in which annual income and net worth are calculated for purposes of determining accredited investor status.[57] As in the proposal,

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54 For a more detailed discussion of survival rates for startups and small businesses see Section III.A, below.

55 *See* Instruction 3 to paragraph (a)(2) of Rule 100 of Regulation Crowdfunding.

56 *See* Instruction 1 to paragraph (a)(2) of Rule 100 of Regulation Crowdfunding.

57 17 CFR §230.501. Thus, for example, a natural person's primary residence shall not be included as an asset in the calculation of net worth. 17 CFR §230.501(a)(5)(i)(A).

the final rules allow spouses to calculate their net worth or annual income jointly. Although some commenters opposed permitting net worth or annual income to be calculated jointly, we believe this approach is appropriate in light of the stricter investment limits being adopted in the final rules. Several commenters recommended that, if the final rules permit net worth and annual income to be calculated jointly, we should establish an aggregate investment limit applicable to both spouses.[58] Consistent with this recommendation, the final rules add an instruction to explain that when such a joint calculation is used, the aggregate investment of the spouses may not exceed the limit that would apply to an individual investor at that income and net worth level.[59] We believe this approach is necessary to preserve the intended protections of the investment limits.

While a number of commenters supported the creation of a different investment limit for accredited or institutional investors, or exempting them altogether, we are not making such a change. As noted above, crowdfunding is an innovative approach to raising capital in which the entity or individual raising capital typically seeks small individual contributions from a large number of people. As such, we believe that crowdfunding transactions were intended under Section 4(a)(6) to be available equally to all types of investors.[60] The statute provides specific investment limits, and the only reference in the statute to changing those investment limits is the requirement that we update the investment limits not less frequently than every five years based

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58 *See* Brown J. Letter; Consumer Federation Letter; Fund Democracy Letter; Jacobs Letter.

59 For example, if each spouse's annual income is $30,000, the spouses jointly may invest up to an aggregate of 5% of their joint income of $60,000. If one spouse's annual income is $120,000 and the other's is $30,000, the spouses jointly may invest up to an aggregate of 10% of their joint income of $150,000, the same investment limit that would apply for an individual investor with income of $150,000. *See* Instruction 2 to paragraph (a)(2) of Rule 100 of Regulation Crowdfunding.

60 *See* 158 CONG. REC. S1689 (daily ed. Mar. 15, 2012) (statement of Sen. Mark Warner ("There is now the ability to use the Internet as a way for small investors to get the same kind of deals that up to this point only select investors have gotten that have been customers of some of the best known investment banking firms, where we can now use the power of the Internet, through a term called crowdfunding.").

on the Consumer Price Index. Further, issuers can rely on other exemptions to offer and sell securities to accredited investors and institutional investors. As discussed above, concurrent offerings to these types of investors are possible if the conditions of each applicable exemption are met.[61] Therefore, we are not altering the investment limits for any particular type of investor or to create a different exemption based on different investment limits. Thus, as proposed, the investment limits will apply equally to all investors, including retail, institutional and accredited investors.

3. Transaction Conducted Through an Intermediary

a. Proposed Rules

Section 4(a)(6)(C) requires that a transaction in reliance on Section 4(a)(6) be conducted through a broker or funding portal that complies with the requirements of Securities Act Section 4A(a). To implement this provision, we proposed in Rule 100(a)(3) of Regulation Crowdfunding that for any transaction conducted in reliance on Section 4(a)(6), an issuer use only one intermediary (that complies with the requirements of Section 4A(a) and the related requirements in Regulation Crowdfunding) and that the transaction be conducted exclusively on the intermediary's platform. We also proposed to permit the intermediary to engage in back office[62] or other administrative functions other than on the intermediary's platform, and to define "platform" as "an Internet website or other similar electronic medium through which a registered broker or a registered funding portal acts as an intermediary in a transaction involving the offer or sale of securities in reliance on Section 4(a)(6)."

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61 For a discussion of integration, see Section II.A.1.c.

62 Back office personnel typically perform functions such as, but not limited to, recordkeeping, trade confirmations, internal accounting, and account maintenance.

b. Comments on the Proposed Rules

Commenters were divided about the proposed prohibition on an issuer using more than one intermediary for any transaction conducted pursuant to Section 4(a)(6). Supporters of the proposed prohibition expressed the view that the prohibition would benefit communication between issuers and investors.[63] One commenter stated that the prohibition also would assist in assessing whether investors are within their investment limits.[64] Commenters who opposed the proposed prohibition noted that increasing the number of platforms used per transaction would both increase the likelihood of investors becoming informed that a transaction is taking place, as well as elicit information from a more diverse crowd.[65]

Commenters were generally divided about the proposed requirement that transactions made in reliance on Section 4(a)(6) be conducted exclusively through the intermediary's platform. Commenters who supported[66] the proposed requirement cited concerns that allowing the transactions to be effected through means other than the intermediary's platform could increase the potential for fraudulent activity[67] and prevent the leveraging of information sharing and crowdsourced review that are intended through crowdfunding.[68] Commenters who opposed[69] the proposed requirement expressed their view that permitting other means would allow persons who lack Internet access to invest through crowdfunding,[70] and also would foster different types of in-

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63 *See, e.g.*, CFA Institute Letter; Rockethub Letter.

64 *See* CFA Institute Letter.

65 *See, e.g.*, Graves Letter.

66 *See, e.g.*, Joinvestor Letter; RoC Letter; RocketHub Letter; Wilson Letter.

67 *See, e.g.*, StartupValley Letter.

68 *See, e.g.*, RocketHub Letter.

69 *See, e.g.*, Benjamin Letter; Omara Letter; Public Startup Letter 2.

70 *See, e.g.*, Projecteureka Letter.

person communication that are not possible to achieve online.[71] One commenter expressed a preference for issuers to be able to host their own offerings subject to certain conditions.[72] One commenter also suggested that intermediaries should be able to engage in certain activities other than on their platforms, such as physically meeting with representatives of issuers and investors, and hosting launch parties.[73]

A few commenters supported, but suggested technical revisions to, our proposed definition of "platform."[74] One commenter suggested deleting the phrase "an Internet website or other similar electronic medium" and replacing the phrase with "a software program accessible via TCP/IP enabled applications" or to more commonly define "platform" as "a software program accessible via the Internet."[75]

c. Final Rules

After considering the comments, we are adopting as proposed Rule 100(a)(3). We also are adopting the definition of "platform" with one clarifying amendment and with a change in location to Rule 300(c).

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71 *See, e.g.*, Benjamin Letter ("Without doubt, the web fosters a crowd and a convenient forum to express ideas and learn about the Issuer. However, small community gatherings provide similar feedback loops and often times serve the community and some investors better by fostering nuanced forms of communication that can never be achieved. Further, some SEC concerns can be assuaged regarding the loss of creating a 'crowd' online because some investors that may rely on the website to educate themselves may not be inclined to contribute to the 'crowd intelligence' online, yet would be vocal in a community gathering.").

72 *See* Public Startup Letter 2. We note that Section 4(a)(6) of the Securities Act requires that, as a condition of the exemption, the transaction be "conducted through a broker or funding portal that complies with the requirements of section 4A(b)." 15 U.S.C. 77d(a)(6).

73 *See* Wilson Letter.

74 *See, e.g.*, Arctic Island Letter 1, Arctic Island Letter 3; Arctic Island Letter 4; and Startup Valley Letter (explaining that websites, application programmable interfaces (APIs) and other electronic media are generally only the means to access a platform, which itself is an Internet-accessible software program).

75 *See* Arctic Island Letter 1; Arctic Island Letter 4 (noting that a "platform" is actually a software program that is accessible via the Internet and that a "website or other electronic medium" is merely a way to access the platform, not the platform itself).

As stated in the Proposing Release, we believe that requiring an issuer to use only one intermediary to conduct an offering or concurrent offerings in reliance on Section 4(a)(6) would help foster the creation of a "crowd" and better accomplish the purpose of the statute. In order for a crowd to effectively share information, we believe it would be most beneficial to have one meeting place for the crowd to obtain and share information, thus avoiding dilution or dispersement of the "crowd." We also believe that limiting a crowdfunding transaction to a single intermediary's online platform helps to minimize the risk that issuers and intermediaries would circumvent the requirements of Regulation Crowdfunding. For example, allowing an issuer to conduct an offering using more than one intermediary would make it more difficult for intermediaries to determine whether an issuer is exceeding the $1 million aggregate offering limit.

We continue to believe that crowdfunding transactions made in reliance on Section 4(a)(6) and activities associated with these transactions should occur over the Internet or other similar electronic medium that is accessible to the public. Such an "online-only" requirement enables the public to access offering information and share information publicly in a way that will allow members of the crowd to share their views on whether to participate in the offering and fund the business or idea. While we acknowledge, as one commenter observed, that there are forms of communication that cannot be achieved online,[76] we nevertheless believe that the requirement that the transaction be conducted exclusively through the intermediary's platform will help to ensure transparency, provide for ready availability of information in one place to all investors, and promote greater uniformity in the distribution of information among investors. We also do not believe that funding portals should be permitted to physically meet with investors to solicit investments and offerings on its platform, or host launch parties, as one commenter recommended,

[76] *See* Benjamin Letter (in-person gatherings may foster more "nuanced forms of communication").

because these activities likely violate the statutory prohibition on funding portals soliciting and providing investment advice and recommendations. However, we continue to believe that intermediaries should be able to engage in back office and other administrative functions other than on their platforms.

In a change from the proposed rules, and consistent with the suggestions of commenters, the final rules define "platform" as "*a program or application accessible via the Internet or other similar electronic communication medium* through which a registered broker or a registered funding portal acts as an intermediary in a transaction involving the offer or sale of securities in reliance on Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6))" [emphasis added].[77] We believe that this definition is more technically accurate and also will accommodate innovation in the event of technological advancements. We are moving the definition of "platform" from Rule 100 to Rule 300(c) so that it will be located alongside the other Regulation Crowdfunding definitions related to intermediaries. Also, in a change from the proposed rule, we are moving to the definition of platform an instruction stating that an intermediary through which a crowdfunding transaction is conducted may engage in back office or other administrative functions other than on the intermediary's platform.[78]

4. Exclusion of Certain Issuers from Eligibility under Section 4(a)(6)

Securities Act Section 4A(f) excludes certain categories of issuers from eligibility to rely on Section 4(a)(6) to engage in crowdfunding transactions. These are: (1) issuers that are not organized under the laws of a state or territory of the United States or the District of Columbia; (2)

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[77] Rule 300(c) of Regulation Crowdfunding.

[78] In the final rule, this is an instruction to Rule 300(c)(4). The instruction was proposed under proposed Rule 100(a)(3), but we believe it is more appropriate under the definition of platform because the instruction explains that back office activities can happen off the platform.

issuers that are subject to Exchange Act reporting requirements;[79] (3) investment companies as defined in the Investment Company Act of 1940 (the "Investment Company Act")[80] or companies that are excluded from the definition of investment company under Section 3(b) or 3(c) of the Investment Company Act;[81] and (4) any other issuer that the Commission, by rule or regulation, determines appropriate.

a. Proposed Rules

Rule 100(b) of Regulation Crowdfunding, as proposed, would exclude the categories of issuers specifically identified in Section 4A(f). In addition, the proposed rules would exclude: (1) issuers that are disqualified from relying on Section 4(a)(6) pursuant to the disqualification provision in Rule 503(a) of Regulation Crowdfunding; (2) issuers that have sold securities in reliance on Section 4(a)(6) if they have not filed with the Commission and provided to investors, to the extent required, the ongoing annual reports required by Regulation Crowdfunding during the two years immediately preceding the filing of the required new offering statement; and (3) issuers that have no specific business plan or that have indicated that their business plan is to engage in a merger or acquisition with an unidentified company or companies.

b. Comments on the Proposed Rules

Foreign Issuers, Exchange Act Reporting Companies, and Investment Companies. Several commenters opposed the exclusion of foreign issuers, Exchange Act reporting companies, and investment companies.[82] Other commenters, however, supported the exclusion of investment

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79 These are issuers who are required to file reports with the Commission pursuant to Exchange Act Sections 13(a) (15 U.S.C. 78m(a)) or 15(d) (15 U.S.C. 78*o*(d)).

80 15 U.S.C 80a-1 *et seq*.

81 15 U.S.C. 80a-3(b) or (c).

82 *See, e.g.*, M.A.V. Letter (opposing the exclusion of public companies from eligibility to rely on Section 4(a)(6)); Ritter Letter (asking for clarification regarding companies that are excluded from the definition of

companies or companies that are excluded from the definition of investment company under Section 3(b) or 3(c) of the Investment Company Act.[83] Some commenters recommended that, despite the exclusion of investment companies, the Commission allow a single purpose fund, including LLCs and LPs, to conduct an offering in reliance on Section 4(a)(6) if such fund were organized to invest in, or lend money to, a single company.[84]

Delinquent in Ongoing Reporting. A number of commenters supported the exclusion of issuers that are delinquent in their reporting obligations,[85] although others opposed the exclusion of delinquent issuers.[86] Some commenters suggested options such as disclosure of the issuer's reporting delinquency in its offering documents or on its website or a cure provision.[87]

We also received comments about whether the exclusion should extend to issuers that are delinquent in other reporting requirements (e.g., updates on the progress of the issuer in meeting the target offering amount, issuers whose affiliates have failed to comply with the ongoing reporting requirements, and issuers with an officer, director, or controlling shareholder who

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investment company pursuant to 3(b) of the Investment Company Act); TAN Letter (opposing the exclusion of foreign issuers over concerns that investors would not have Title III protections when investing in foreign issuers and that investors' ability to invest in early opportunities would be reduced).

83 *See, e.g.*, Commonwealth of Massachusetts Letter; PeoplePowerFund Letter.

84 *See, e.g.*, EMKF Letter (stating that having hundreds of direct shareholders can give startups "messy cap tables" that deter follow-on financing and alternatively recommending the Commission permit an intermediary, including a funding portal, to act as a holder of record); Fryer Letter; Growthfountain Letter; Martin Letter (recommending that crowdfunding be operated through a trust fund mechanism that would own shares of the entity seeking capital); Propellr Letter 2; Ritter Letter; Wefunder Letter.

85 *See, e.g.*, ASSOB Letter; Commonwealth of Massachusetts Letter; Consumer Federation Letter; Fund Democracy Letter; Grassi Letter; Joinvestor Letter; NASAA Letter; Wefunder Letter.

86 *See, e.g.*, ABA Letter; Parsont Letter; Projectheureka Letter; Public Startup Letter 2; RocketHub Letter.

87 *See, e.g.*, ABA Letter (suggesting a reasonable cure period and limiting the "look-back" period to one year); Grassi Letter (recommending that a delinquent issuer be required to file a form with the Commission and publish on its website and the relevant intermediary's platform a notice to potential investors that it has not met its reporting obligations); Parsont Letter (recommending the Commission treat the ongoing reporting requirements as a condition to the Section 4(a)(6) exemption and create a notice and cure provision in the proposed insignificant deviation safe harbor); RocketHub Letter (suggesting delinquent issuers be required to disclose their delinquent status in their offering documents); Vann Letter (recommending a grace period for curing the deficiency).

served in a similar capacity with another issuer that failed to file its ongoing reports). Commenters generally opposed extending the exclusion beyond issuers delinquent in their ongoing annual reports during the two years immediately preceding the filing of the required new offering statement.[88] Further, two commenters opposed the idea of excluding an issuer whose officer, director, or controlling shareholder served in a similar capacity with another issuer that failed to file its annual reports.[89]

Business Plans. Commenters were divided on excluding issuers that have no specific business plan from eligibility to rely on Section 4(a)(6).[90] Commenters, however, supported the exclusion of issuers that have business plans to engage in a merger or acquisition with an unidentified company.[91]

c. Final Rules

We are adopting the issuer eligibility requirements as proposed, with the addition of two clarifications. As noted above, Section 4A(f) expressly excludes foreign issuers, Exchange Act reporting companies and companies that are investment companies as defined in the Investment Company Act or companies that are excluded from the definition of investment company under Section 3(b) or 3(c) of the Investment Company Act from the exemption for crowdfunding

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88 *See, e.g.*, Grassi Letter (stating that further exclusions would impose a more onerous burden on issuers under Section 4(a)(6) than that placed on current registrants filing under Exchange Act Sections 13(a) or 15(d) or emerging growth companies); Projectheureka Letter.

89 *See* Grassi Letter (stating that these persons may not have the authority or responsibility to file an annual report); Whitaker Chalk Letter.

90 For commenters who expressed support, *see, e.g.*, Anonymous Letter 2; CFA Institute Letter; CFIRA Letter 7; Commonwealth of Massachusetts Letter; Consumer Federation Letter; Hackers/Founders Letter; NASAA Letter; ODS Letter; Traklight Letter; Whitaker Chalk Letter. For commenters who expressed opposition, *see, e.g.*, ABA Letter (expressing concern that a particular business idea disclosed by a crowdfunding issuer might be deemed after-the-fact to be too non-specific to have permitted reliance on Section 4(a)(6), thus exposing that issuer to a potential Section 5 violation); FundHub Letter 1; Projectheureka Letter; Public Startup Letter 2; RoC Letter; RocketHub Letter; SBM Letter; Wilson Letter.

91 *See, e.g.*, ABA Letter; CFA Institute Letter; Commonwealth of Massachusetts Letter; Consumer Federation Letter; Grassi Letter; ODS Letter; RFPIA Letter.

transactions provided by Section 4(a)(6). Although some commenters expressed concerns about these statutory exclusions, including that such exclusions could limit the investment choices of crowdfunding investors, we are not creating additional exemptions for these categories of issuers. In reaching this determination, we have considered that the primary purpose of Section 4(a)(6), as we understand it, is to facilitate capital formation by early stage companies that might not otherwise have access to capital.[92] As a general matter, we do not believe that Exchange Act reporting companies, investment companies and foreign issuers accessing the U.S. capital markets constitute the types of issuers that Section 4(a)(6) and Regulation Crowdfunding are intended to benefit. Moreover, we believe that certain of these issuers, such as foreign issuers or investment companies, may present unique risks that would make them unsuitable for the scaled regulatory regime associated with securities-based crowdfunding transactions. Accordingly, the final rules exclude these categories of issuers from Regulation Crowdfunding.[93]

We are not creating, as suggested by some commenters,[94] an exception to this exclusion for a single purpose fund organized to invest in, or lend money to, a single company. The statute specifically excludes investment funds from eligibility to rely on Section 4(a)(6) and investment fund issuers present considerations different from those for non-fund issuers.

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92 *See, e.g.*, 158 Cong. Rec. S1765 (daily ed. Mar. 29, 2012) (statement of Sen. Jack Reed) ("[Crowdfunding] is the place where we envision the smallest entrepreneurs could obtain much needed seed capital for their good ideas."); 158 Cong. Rec. H1581 (daily ed. Mar. 27, 2012) (statement of Rep. Patrick McHenry ("Crowdfunding is the best of microfinancing and crowdsourcing. You use a wide network of individuals and you can raise capital for your new business, your start-up, or your small business.").

93 See Rule 100(b) of Regulation Crowdfunding.

94 *See, e.g.*, EMKF Letter; Fryer Letter; Growthfountain Letter; Martin Letter; Propellr Letter 2; Wefunder Letter.

In addition to these statutorily excluded categories of issuers, the final rules also exclude, as proposed, several additional categories of issuers. Below we discuss each of these additional categories:

Disqualification Provisions. As discussed further in Section II.E.6 below, the final rules also exclude issuers that are disqualified from relying on Section 4(a)(6).[95]

Delinquent in Ongoing Reporting. Consistent with the proposed rules and the views of a number of commenters,[96] the final rules exclude an issuer that has sold securities in reliance on Section 4(a)(6) if the issuer has not filed with the Commission and provided to investors, to the extent required, the ongoing annual reports required by Regulation Crowdfunding[97] during the two years immediately preceding the filing of the required new offering statement.[98] As discussed further in Section II.B.2 below, we believe that the annual ongoing reporting requirement will benefit investors by enabling them to consider updated information about the issuer, thereby allowing them to make more informed investment decisions. If issuers fail to comply with this requirement, we do not believe that they should have the benefit of relying on the exemption under Section 4(a)(6) again until they file, to the extent required, the two most recent annual reports.[99] In addition, as discussed further in Section II.B.1 below, in a modification to the

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95 *See* Rule 100(b)(4) of Regulation Crowdfunding. *See also* Rule 503 of Regulation Crowdfunding and Section II.E.6 for a discussion of the disqualification provisions.

96 *See, e.g.*, ASSOB Letter; Commonwealth of Massachusetts Letter; Consumer Federation Letter; Fund Democracy Letter; Grassi Letter; Joinvestor Letter; NASAA Letter; Wefunder Letter.

97 *See* Rules 202 and 203(b) of Regulation Crowdfunding and Section II.B.2 for a discussion of the ongoing reporting requirements.

98 *See* Rule 100(b)(5) of Regulation Crowdfunding.

99 We note that even if an issuer has regained eligibility to rely on Regulation Crowdfunding, the Commission could still bring an enforcement action under the federal securities laws based on the issuer's failure to make the required filings. In addition, as discussed in Section II.E.4., new Rule 12g-6 provides an exemption from Section 12(g) conditioned, among other things, on the issuer's compliance with the annual reporting requirements of Rule 202 of Regulation Crowdfunding.

proposed rules, the final rules require an issuer to disclose in its offering statement and annual report if it, or any of its predecessors, previously failed to comply with the ongoing reporting requirements of Regulation Crowdfunding.

We note that some commenters read the provision requiring issuers to have filed their two most recent annual reports to mean that the disqualification would be triggered only after the issuer was delinquent for two consecutive years or that an issuer would be disqualified for two years.[100] Instead, the final rule requires that any ongoing annual report that was due during the two years immediately preceding the currently contemplated offering must be filed before an issuer may rely on the Section 4(a)(6) exemption. For example, if more than 120 days have passed since the issuer's fiscal year end and the issuer has not filed the required annual report for that most recently ended fiscal year, the issuer will not be able to conduct a new offering of securities in reliance on the Section 4(a)(6) exemption until the delinquent annual report has been filed. Similarly, if an issuer did file an annual report for the most recently ended fiscal year but did not file an annual report for the fiscal year prior to that, the issuer will not be able to rely on the Section 4(a)(6) exemption until the missing report has been filed. In both cases, as soon as the issuer has filed with the Commission and provided to investors both of the annual reports required during the two years immediately preceding the filing of the required offering statement, the issuer will be able to rely on the Section 4(a)(6) exemption. The final rule text includes an instruction to clarify this requirement.[101]

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[100] *See, e.g.*, Consumer Federation Letter; Fund Democracy Letter; NASAA Letter.

[101] *See* instruction to paragraph (b)(5) of Rule 100 of Regulation Crowdfunding

Consistent with the proposal and the recommendations of commenters,[102] we are not extending the exclusion to issuers that are delinquent in the progress update or termination of reporting requirements, nor are we excluding issuers whose officer, director, or controlling shareholder served in a similar capacity with another issuer that failed to file its annual reports. Extending the exclusion to those issuers would impose more stringent requirements than those faced by current reporting companies and issuers under Regulation A.

Business Plans. The final rules also exclude an issuer that has no specific business plan or has indicated that its business plan is to engage in a merger or acquisition with an unidentified company or companies.[103] We believe that the exemption under Section 4(a)(6) is intended to provide an issuer with an early stage project, idea or business an opportunity to share it publicly with a wider range of investors. Those investors may then share information with each other about the opportunity and use that information to decide whether or not to invest. Thus, we believe that an issuer engaging in crowdfunding under the exemption should give the public sufficient information about a particular proposed project or business to allow investors to make an informed investment decision.[104]

As discussed in the proposal, we are cognizant of the challenges noted by some commenters[105] in distinguishing between early-stage proposals that have information sufficient to support the crowdfunding mechanism and those that cannot by their terms do so. After

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102 *See, e.g.*, Grassi Letter; Projectheureka Letter; Whitaker Chalk Letter.

103 *See* Rule 101(b)(6) of Regulation Crowdfunding.

104 *See, e.g.*, Section 4A(b)(1)(C) (requiring a description of the business of the issuer and the anticipated business plan of the issuer).

105 S*ee, e.g.*, ABA Letter; FundHub Letter 1; Projectheureka Letter; Public Startup Letter 2; RoC Letter; RocketHub Letter; SBM Letter; Wilson Letter.

considering the comments received,[106] we continue to believe that the rules should exclude issuers that have no specific business plan or whose business plan is to engage in a merger or acquisition with an unidentified company or companies. We understand that issuers engaging in crowdfunding transactions may have businesses at various stages of development in differing industries, and therefore, we believe that a specific "business plan" for such issuers could encompass a wide range of project descriptions, articulated ideas, and business models.

Overall, we believe that the exclusions in the final rules appropriately consider the need to limit the potential risks to investors that could result from extending issuer eligibility to certain types of entities without unduly limiting the benefits of the exemption as a tool for capital formation.

B. Issuer Requirements

1. Disclosure Requirements

Securities Act Section 4A(b)(1) sets forth specific disclosures that an issuer offering or selling securities in reliance on Section 4(a)(6) must "file with the Commission and provide to investors and the relevant broker or funding portal, and make available to potential investors". These disclosures include:

- the name, legal status, physical address and website address of the issuer;[107]
- the names of the directors and officers (and any persons occupying a similar status or performing a similar function), and each person holding more than 20 percent of the shares of the issuer;[108]

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[106] *See, e.g.*, ABA Letter; Anonymous Letter 2; CFA Institute Letter; CFIRA Letter 7; Commonwealth of Massachusetts Letter; Consumer Federation Letter; FundHub Letter 1; Grassi Letter; Hackers/Founders Letter; NASAA Letter; ODS Letter; Projectheureka Letter; Public Startup Letter 2; RFPIA Letter; RoC Letter; RocketHub Letter; SBM Letter; Traklight Letter; Whitaker Chalk Letter; Wilson Letter.

[107] Section 4A(b)(1)(A).

- a description of the business of the issuer and the anticipated business plan of the issuer;[109]
- a description of the financial condition of the issuer;[110]
- a description of the stated purpose and intended use of the proceeds of the offering sought by the issuer with respect to the target offering amount;[111]
- the target offering amount, the deadline to reach the target offering amount and regular updates about the progress of the issuer in meeting the target offering amount;[112]
- the price to the public of the securities or the method for determining the price;[113] and
- a description of the ownership and capital structure of the issuer.[114]

In addition, Section 4A(b)(1)(I) specifies that the Commission may require additional disclosures for the protection of investors and in the public interest.

As discussed further in Section II.B.3 below, we are requiring issuers to file these disclosures with the Commission on Form C.[115] Unless otherwise indicated in the form,

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108 Section 4A(b)(1)(B).

109 Section 4A(b)(1)(C).

110 Section 4A(b)(1)(D).

111 Section 4A(b)(1)(E).

112 Section 4A(b)(1)(F).

113 Section 4A(b)(1)(G).

114 Section 4A(b)(1)(H). Specifically, Section 4A(b)(1)(H) requires a description of: "(i) terms of the securities of the issuer being offered and each other class of security of the issuer…; (ii) a description of how the exercise of the rights held by the principal shareholders of the issuer could negatively impact the purchasers of the securities being offered; (iii) the name and ownership level of each existing shareholder who owns more than 20 percent of any class of the securities of the issuer; (iv) how the securities being offered are being valued…; and (v) the risks to purchasers of the securities relating to minority ownership in the issuer, the risks associated with corporate actions, including additional issuances of shares, a sale of the issuer or of assets of the issuer, or transactions with related parties."

Form C must be filed in the standard format of eXtensible Markup Language (XML). The XML-based fillable portion of Form C will enable issuers to provide information in a convenient medium without requiring the issuer to purchase or maintain additional software or technology. This will provide the Commission and the public with readily available data about offerings made in reliance on Section 4(a)(6). Other required disclosure that is not required to be provided in the XML-based text boxes will be filed as attachments to Form C. We are not mandating a specific presentation format for the attachments to Form C; however, the final Form C does include an optional Q&A format that crowdfunding issuers may use to provide disclosures that are not required to be filed in XML format.[116] We believe that this optional format should help reduce the burden on crowdfunding issuers of preparing disclosures.

By filing Form C with the Commission and providing it to the relevant intermediary, issuers will satisfy the requirement of Securities Act Section 4A(b) that issuers relying on Section 4(a)(6) must "file with the Commission and provide to investors and the relevant broker of funding portal, and make available to potential investors" certain information. In a clarifying change from the proposal, we have moved the definition of "investor" from proposed Rule 300(c)(4) to Rule 100(d) to clarify that for purposes of all of Regulation Crowdfunding, "investor" includes any investor or any potential investor, as the context requires.[117] In connection with this clarifying move we

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115 Issuers will use Form C to provide the required disclosures about the crowdfunding transaction and the information required to be filed annually. *See* Section II.B.3.

116 *See* Item 1 of General Instruction III to Form C of Regulation Crowdfunding.

117 *See* Rule 100(d) of Regulation Crowdfunding.

have deleted the phrase "and make available to potential investors" each time it appeared in the proposed Rules 201 and 203 to avoid redundancy.[118]

Additionally, as we clarify in the final rules, to the extent that some of the required disclosures overlap, issuers are not required to duplicate disclosures.

a. Offering Statement Disclosure Requirements

(1) Information about the Issuer and the Offering

(a) General Information about the Issuer, Officers and Directors, and Certain Shareholders

(i) Proposed Rules

To implement Sections 4A(b)(1)(A) and (B), we proposed in Rule 201 of Regulation Crowdfunding to require an issuer to disclose information about its legal status, directors, officers and certain shareholders and how interested parties may contact the issuer. Specifically, we proposed to require that an issuer disclose:

- its name and legal status, including its form of organization, jurisdiction in which it is organized and date of organization;
- its physical address and its website address; and
- the names of the directors and officers, including any persons occupying a similar status or performing a similar function, all positions and offices with the issuer held by such persons, the period of time in which such persons served in the positions or offices and their business experience during the past three years, including:
    - each person's principal occupation and employment, including whether any officer is employed by another employer; and

[118] *See* Rules 201 and 203(a) of Regulation Crowdfunding.

- the name and principal business of any corporation or other organization in which such occupation and employment took place.

We proposed to define "officer" consistent with the definition in Securities Act Rule 405 and in Exchange Act Rule 3b-2. We further proposed to require disclosure of the business experience of directors and officers of the issuer during the past three years.

Section 4A(b)(1)(B) requires disclosure of "the names of . . . each person holding more than 20 percent of the shares of the issuer." In contrast, Section 4A(b)(1)(H)(iii) requires disclosure of the "name and ownership level of each existing shareholder who owns more than 20 percent *of any class* of the securities of the issuer" (emphasis added). We proposed in Rule 201(c) to require disclosure of the names of persons, as of the most recent practicable date, who are the beneficial owners of 20 percent or more of the issuer's outstanding voting equity securities, calculated on the basis of voting power ("20 Percent Beneficial Owners"). Neither Section 4A(b)(1)(B) nor Section 4A(b)(1)(H)(iii) states as of what date the beneficial ownership should be calculated. We proposed in Rule 201(c) to require issuers to calculate beneficial ownership as of the most recent practicable date.

(ii) Comments on the Proposed Rules

Of the commenters that addressed the proposed issuer, officer and director disclosure rules, some generally supported them,[119] while others opposed specific disclosure requirements. For example, one commenter opposed requiring issuers to disclose a website address.[120] Other commenters opposed requiring issuers to disclose the business experience of their officers and

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119 *See, e.g.*, Angel Letter 1; CCI Letter; Denlinger Letter 1; Mollick Letter; Wefunder Letter; Wilson Letter.

120 *See* Vann Letter (recommending that the disclosure requirement be optional or only required for businesses that have a website).

directors,[121] while one commenter suggested narrowing the definition of the term "officer."[122] Some commenters expressed opposition to any revision to the proposed rules that would require disclosure of any court orders, judgments or civil litigation involving any directors and officers.[123]

Some commenters supported the proposed three-year time period to be covered by the officer and director disclosure rules,[124] while others recommended that officer and director disclosure cover the previous five years.[125] Some commenters recommended we require additional disclosures about an issuer's officers, directors and persons occupying a similar status or performing a similar function.[126]

A few commenters commented on the proposed 20 Percent Beneficial Owner rules. One commenter supported the requirement to disclose the names of persons who are the 20 Percent Beneficial Owners,[127] while one commenter opposed the requirement.[128] One commenter recommended that, to provide greater certainty for investors and more guidance for issuers, the beneficial ownership be calculated as of a specific date, rather than the most recent practicable date, and that the disclosure be updated when there are significant changes in beneficial

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121 *See, e.g.*, Public Startup Letter 2; RocketHub Letter; Schwartz Letter; Zhang Letter.

122 *See* RocketHub Letter (stating that only relevant officers for most companies using Regulation Crowdfunding would be the principal executive officer and the principal financial officer, which may be the same person.)

123 *See, e.g.*, FundHub Letter 1; RocketHub Letter; Wefunder Letter.

124 *See, e.g.*, Denlinger Letter 1; Joinvestor Letter; Wefunder Letter.

125 *See, e.g.*, Commonwealth of Massachusetts Letter; NASAA Letter.

126 *See, e.g.*, Angel Letter 1 (qualifications of candidates for the board of directors); Denlinger Letter 1(educational background of the officers and directors); Mollick Letter (online identities of the officers and directors); ODS Letter (educational background of the officers and directors);Wilson Letter (technical and business skills of the officers and directors); Zeman Letter (any officer and director positions held by the officers and directors or their family members, as well as any 10 percent beneficial holdings they may have with other SEC registrants; and disputes the officers and directors had with other employers).

127 *See* RocketHub Letter.

128 *See* Public Startup Letter 2.

ownership.[129] Finally, one commenter recommended that the Commission keep the requirement as simple as possible.[130]

(iii) Final Rules

We are adopting the issuer, officer and director, and 20 Percent Beneficial Owners disclosure requirements largely as proposed.[131] An issuer will be required to disclose information about its president, vice president, secretary, treasurer or principal financial officer, comptroller or principal accounting officer and any person routinely performing similar functions. As noted by at least one commenter,[132] an issuer may not have officers serving in each of these roles. Accordingly, the final rules require the disclosure only to the extent an issuer has individuals serving in these capacities or performing similar functions.[133] The required information includes all positions and offices held with the issuer, the period of time in which such persons served in the position or office and their prior business experience.[134] Contrary to the views of some commenters,[135] we believe that additional disclosures about an issuer's officers, directors and persons occupying a similar status or performing a similar function would be unduly burdensome and generally not necessary for investors to be in a position to make an informed investment decision. Given the diverse nature of the startups and small businesses that we anticipate will

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129 *See* NASAA Letter.

130 *See* RocketHub Letter.

131 *See* Rule 201(a)-(c) of Regulation Crowdfunding.

132 *See* RocketHub Letter.

133 *See* Instruction to paragraph (b) of Rule 201 of Regulation Crowdfunding.

134 *See* Rule 201(b) of Regulation Crowdfunding.

135 *See, e.g.*, Denlinger 1 Letter (educational background of officers); ODS Letter (educational background of officers, directors and similar persons); Zeman Letter (proposing that officers and directors of an issuer be required to disclose their (or family members) officer and director positions with other SEC registrants, and disclose material holdings of more than 10% with other SEC registrants).

seek to raise capital in reliance on Section 4(a)(6), additional disclosures such as those recommended by some commenters may not be relevant in all instances.

The required disclosure about the business experience of the directors and officers (and any persons occupying a similar status or performing a similar function) must cover the past three years,[136] which, as some commenters noted,[137] is shorter than the five-year period that applies to issuers conducting registered offerings[138] or exempt offerings pursuant to Regulation A.[139] We believe that startups and small businesses that may seek to raise capital in reliance on Section 4(a)(6) generally will be smaller than the issuers conducting registered offerings or exempt offerings pursuant to Regulation A, and generally are likely to have a more limited operating history.[140] Therefore, in comparison to registered offerings and Regulation A, we believe the three-year period is more relevant given the stage of development of these issuers and should help to reduce compliance costs for issuers conducting offerings pursuant to Section 4(a)(6) while still providing investors with sufficient information about the business experience of directors and officers of the issuer to make an informed investment decision.

Notwithstanding the suggestion of one commenter, and consistent with the statute, the final rules require disclosure of an issuer's website.[141] Given the Internet-based nature of Crowdfunding, we anticipate that every issuer will have a website or be able to create one at a minimal cost.

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136 *See* Rule 201(b) of Regulation Crowdfunding.

137 *See, e.g.*, Commonwealth of Massachusetts Letter; NASAA Letter.

138 *See* Item 401(e) of Regulation S-K [17 CFR 229.401(e)].

139 *See* Item 8(c) of Form 1-A [17 CFR 239.90].

140 There is no limit on the amount of proceeds that may be raised in a registered offering, and Regulation A permits offerings of up to $50 million of securities annually.

141 *See* Rule 201(a) of Regulation Crowdfunding.

We also are adopting the 20 Percent Beneficial Owner disclosure requirement as proposed with one modification.[142] Instead of requiring issuers to disclose the name of each 20 Percent Beneficial Owner as of the most recent practicable date, we are requiring such disclosure as of the most recent practicable date, but no earlier than 120 days prior to the date the offering statement or report is filed. We believe that this change should address commenter concerns[143] about the discretion afforded by the proposed "most recent practicable date." While we are not adding to Rule 201(c) a specific requirement that the disclosure be updated when there are significant changes in beneficial ownership, as requested by one commenter,[144] to the extent a material change in beneficial ownership takes place during the offering, an issuer would be required to file an amended offering statement on Form C/A: Amendment.

As stated in the Proposing Release, we believe that the universe of 20 Percent Beneficial Owners should be the same for the disclosure requirements and the disqualification provisions[145] because this would ease the burden on issuers by requiring them to identify only one set of persons who would be the subject of these rules. We continue to believe that assessing beneficial ownership based on total outstanding voting securities is consistent with Section 4A(b)(1)(B). Section 4A(b)(1)(B) is not limited to voting equity securities, but we believe the limitation is necessary to clarify how beneficial ownership should be calculated since issuers could potentially have multiple classes of securities with different voting powers.

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142 *See* Rule 201(c) of Regulation Crowdfunding.

143 *See* NASAA Letter.

144 *Id*.

145 *See* Rule 503 of Regulation Crowdfunding and Section II.E.6 for a discussion of the disqualification provisions.

(b) Description of the Business

(i) Proposed Rules

Consistent with Section 4A(b)(1)(C), we proposed in Rule 201(d) of Regulation Crowdfunding to require an issuer to disclose information about its business and business plan. The proposed rules did not specify the disclosures that an issuer would need to include in the description of the business and the business plan.

(ii) Comments on the Proposed Rules

While several commenters expressed concerns about requiring an issuer to disclose a description of its business and business plan,[146] most commenters supported this proposed requirement.[147] Some commenters recommended that the disclosure include specific items, such as disclosure of any material contracts of the issuer, any material litigation or any outstanding court order or judgment affecting the issuer or its property;[148] the issuer's business value proposition, revenue model, team, regulatory issues and executive compensation;[149] how the issuer will build value for the shareholders;[150] and plans for implementation, concrete next steps, outside recommendations about the validity of the business, backgrounds of the individuals

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146 *See, e.g.*, ABA Letter; ASSOB Letter; Public Startup Letter 2; Traklight Letter.

147 *See, e.g.*, Anonymous Letter 2; Arctic Island Letter 5; Benjamin Letter; CFIRA Letter 7; Consumer Federation Letter; EMKF Letter; Hackers/Founders Letter; Mollick Letter; NFIB Letter; RocketHub Letter; Saunders Letter; Wefunder Letter.

148 *See, e.g.*, Arctic Island Letter 4 (referencing only pending litigation); Arctic Island Letter 5 (referencing only threatened or pending litigation); FundHub Letter 1; Wilson Letter.

149 *See, e.g.*, Arctic Island Letter 5.

150 *See, e.g.*, Hackers/Founders Letter.

involved and prototypes or concept drawings.[151] One commenter recommended that the disclosure requirement be scaled to match the size of the offering.[152]

Some commenters recommended that the Commission provide a non-exclusive list of the types of information an issuer should consider disclosing, templates, examples or other guidance to assist the issuer in complying with this disclosure requirement.[153] One commenter recommended that the Commission not specify the information to be included in the description of the business or the business plan.[154] Commenters also opposed revising the proposed business description requirement to require the description to include the information requirements of Items 101(a)(2) and 101(h)[155] of Regulation S-K.[156]

(iii) Final Rules

Consistent with the proposal, Rule 201(d) requires an issuer to disclose information about its business and business plan. We are not modifying the proposed rule, as some commenters recommended,[157] to specify the disclosures that an issuer must include in the description of the business and the business plan or to provide a non-exclusive list of the types of information an issuer should consider disclosing. We anticipate that issuers engaging in crowdfunding transactions may have businesses at various stages of development in different industries, and

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151 *See, e.g.*, Mollick Letter.

152 *See* Consumer Federation Letter.

153 *See, e.g.*, ABA Letter; Benjamin Letter; CFIRA Letter 7; Commonwealth of Massachusetts Letter; FundHub Letter 1 (recommending a safe harbor list of requirements); Traklight Letter; Wilson Letter (recommending a checklist or prescribed list of questions).

154 *See* RocketHub Letter.

155 17 CFR 229.101.

156 *See, e.g.*, Hamilton Letter; Public Startup Letter 2; RocketHub Letter.

157 *See, e.g.*, ABA Letter; Arctic Island Letter 4; Arctic Island Letter 5; Benjamin Letter; CFIRA Letter 7; Commonwealth of Massachusetts Letter; FundHub Letter 1; Hackers/Founders Letter; Mollick Letter; Traklight Letter; Wilson Letter.

therefore, we believe that the rules should provide flexibility for these issuers regarding what information they disclose about their businesses. This flexible approach is consistent with the suggestion of one commenter that the business plan requirements be scaled to match the size of the offering.[158] We also are concerned that a non-exclusive list of the types of information an issuer should consider providing would be viewed as a *de facto* disclosure requirement that all issuers would feel compelled to meet and would, therefore, undermine the intended flexibility of the final rules.

(c) Use of Proceeds

(i) Proposed Rules

Consistent with Section 4A(b)(1)(E), we proposed in Rule 201(i) of Regulation Crowdfunding to require an issuer to provide a description of the purpose of the offering and intended use of the offering proceeds. We expected that such disclosure would provide a sufficiently detailed description of the intended use of proceeds to permit investors to evaluate the investment. Under the proposed rules, if an issuer did not have definitive plans for the proceeds, but instead had identified a range of possible uses, then the issuer would be required to identify and describe each probable use and factors affecting the selection of each particular use. In addition, if an issuer indicated that it would accept proceeds in excess of the target offering amount,[159] the issuer would be required to provide a separate, reasonably detailed description of the purpose and intended use of any excess proceeds with similar specificity.

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158 *See* Consumer Federation Letter.

159 *See* Section II.B(1)(d) below for a description of the final rule's disclosure requirements with respect to target amounts.

(ii) Comments on the Proposed Rules

Most commenters supported the requirement that issuers disclose the intended use of the offering proceeds.[160] One commenter recommended that we prescribe the use of proceeds disclosure or provide a list of examples that issuers should consider when providing such disclosures.[161] Others recommended a variety of circumstances under which an issuer should be required to update the use of proceeds disclosure.[162]

(iii) Final Rules

We are adopting the use of proceeds disclosure requirement substantially as proposed in Rule 201(i). An issuer will be required to provide a reasonably detailed description of the purpose of the offering, such that investors are provided with enough information to understand how the offering proceeds will be used.[163] While one commenter[164] recommended that we prescribe this disclosure or provide a list of examples, we believe a more prescriptive rule would not best accommodate a diverse range of issuers. Instead, below we provide several examples of the disclosures issuers should consider making with respect to various uses of proceeds.

The disclosure requirement is designed to provide investors with sufficient information to evaluate the investment. For example, an issuer may intend to use the proceeds of an offering to acquire assets or businesses, compensate the intermediary or its own employees or repurchase

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160 *See, e.g.*, ABA Letter; ASSOB Letter; Consumer Federation Letter; Joinvestor Letter; Saunders Letter; Traklight Letter; Whitaker Chalk Letter; Wilson Letter. *But see*, Public Startup Letter 2.

161 *See* Commonwealth of Massachusetts Letter.

162 *See, e.g.*, ASSOB Letter (five percent change); CFIRA Letter 7 (material deviations in the offering statement and any deviations in the annual report); Commonwealth of Massachusetts Letter (material change); Joinvestor Letter (substantial change); RocketHub Letter (significant change); Traklight Letter (material deviations); Whitaker Chalk Letter (material change); Wilson Letter (any deviation). *See* also Section II.B.3 for discussion of when an amendment to the offering statement may be required.

163 *See* Instruction to paragraph (i) of Rule 201 of Regulation Crowdfunding.

164 *See* Commonwealth of Massachusetts Letter.

outstanding securities of the issuer. In providing its description, an issuer would need to consider the appropriate level of detail to provide investors about the assets or businesses that the issuer anticipates acquiring, based on its particular facts and circumstances, so that the investors could make informed decisions. If the proceeds will be used to compensate existing employees or to hire new employees, the issuer should consider disclosing whether the proceeds will be used for salaries or bonuses and how many employees it plans to hire, as applicable. If the issuer will repurchase outstanding issuer securities, it should consider disclosing its plans, terms and purpose for repurchasing the securities. An issuer also should consider disclosing how long the proceeds will satisfy the operational needs of the business. If an issuer does not have definitive plans for the proceeds, but instead has identified a range of possible uses, then the issuer should identify and describe each probable use and the factors the issuer may consider in allocating proceeds among the potential uses.[165] If an issuer indicates that it will accept proceeds in excess of the target offering amount, the issuer must provide a reasonably detailed description of the purpose, method for allocating oversubscriptions, and intended use of any excess proceeds with similar specificity.[166]

(d) Target Offering Amount and Deadline

(i) Proposed Rules

Consistent with Section 4A(b)(1)(F), we proposed in Rule 201(g) of Regulation Crowdfunding to require issuers to disclose the target offering amount and the deadline to reach the target offering amount. In addition, we proposed in Rule 201(h) to require an issuer to disclose whether it would accept investments in excess of the target offering amount, and, if it

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165 *See* Instruction to paragraph (i) of Rule 201 of Regulation Crowdfunding.

166 *See* Instruction to paragraph (i) of Rule 201 of Regulation Crowdfunding.

would, we proposed to require the issuer to disclose, at the commencement of the offering, the maximum amount it would accept. The issuer also, under proposed Rule 201(h), would be required to disclose, at the commencement of the offering, how shares in oversubscribed offerings would be allocated. We further proposed in Rule 201(j) to require issuers to describe the process to cancel an investment commitment or to complete the transaction once the target amount is met, including a statement that:

- investors may cancel an investment commitment until 48 hours prior to the deadline identified in the issuer's offering materials;[167]
- the intermediary will notify investors when the target offering amount has been met;
- if an issuer reaches the target offering amount prior to the deadline identified in its offering materials, it may close the offering early if it provides at least five business days' notice prior to that new deadline (absent a material change that would require an extension of the offering and reconfirmation of the investment commitment);[168] and
- if an investor does not cancel an investment commitment before the 48-hour period prior to the offering deadline, the funds will be released to the issuer upon closing of the offering and the investor will receive securities in exchange for his or her investment.

In addition, proposed Rule 201(k) would require issuers to disclose that if an investor does not reconfirm his or her investment commitment after a material change is made to the offering,

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[167] Section II.C.6 further discusses the cancellation provisions.

[168] *Id.*

the investor's investment commitment will be cancelled and committed funds will be returned. Proposed Rule 201(g) also would require issuers to disclose that if the sum of the investment commitments does not equal or exceed the target offering amount at the time of the offering deadline, no securities will be sold in the offering, investment commitments will be cancelled and committed funds will be returned.[169]

(ii) Final Rules

Commenters were supportive of the proposed rules, and we are adopting the target offering amount and deadline disclosure rules as proposed.[170] As an example of how the final rules will apply, if an issuer sets a target offering amount of $80,000 but is willing to accept up to $650,000, the issuer will be required to disclose both the $80,000 target offering amount and the $650,000 maximum offering amount that it will accept.[171] In an instance where an issuer reaches the target offering amount prior to the deadline identified in its offering materials, it may close the offering early if it provides at least five business days' notice about the new offering deadline as set forth in Rules 201(j) and 302(d) of Regulation Crowdfunding. Accelerating the deadline would not require an extension of the offering and reconfirmation of the investment commitment; however,

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169 *See* Section 4A(a)(7) (requiring intermediaries to "ensure that all offering proceeds are only provided to the issuer when the aggregate capital raised from all investors is equal to or greater than a target offering amount….") and discussion in Section II.C.6.

170 *See* Rules 201(g), 201(h), 201(j) and 201(k) of Regulation Crowdfunding.

171 The issuer in this case also will need to disclose the intended use of the additional proceeds. *See* Instruction to paragraph (i) of Rule 201 of Regulation Crowdfunding. *See also* Section II.B.1.a.i(c) above. In addition, the issuer in this case will be required to provide financial statements reviewed by an independent public accountant (rather than certain tax return information for the most recently completed fiscal year and financial statements certified by the principal executive officer). *See* Section II.B.1.a.ii for a discussion of the financial statement requirements.

issuers would need to consider whether any material change occurred that would require an extension and reconfirmation from investors.[172]

We do not believe it is necessary for us to prescribe how oversubscribed offerings must be allocated if the issuer is required to disclose, at the commencement of the offering, how shares in oversubscribed offerings will be allocated. Commenters were supportive of this approach,[173] and we believe this disclosure should provide investors with important information while maintaining flexibility for issuers to structure the offering as they believe appropriate.

We believe that investors in a crowdfunding transaction will benefit from clear disclosure about their right to cancel, the circumstances under which an issuer may close an offering early and the need to reconfirm the investment commitment under certain circumstances, as they will be more aware of their rights to rescind an investment commitment. Therefore, we are adopting disclosure requirements covering these points, as proposed.

(e) Offering Price

Consistent with Section 4A(b)(1)(G), we proposed in Rule 201(l) of Regulation Crowdfunding to require an issuer to disclose the offering price of the securities or, in the alternative, the method for determining the price, so long as before the sale each investor is provided in writing the final price and all required disclosures.

Commenters were supportive of the proposed disclosure[174] and we are adopting the offering price disclosure rules as proposed.[175] We believe that disclosure of the price or the

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172 Section II.B.1.c discusses the amendment and reconfirmation requirements.

173 *See, e.g.*, CFA Institute Letter; RoC Letter; RocketHub Letter; Wilson Letter.

174 *See, e.g.*, CFA Institute Letter; Wilson Letter. As discussed below, however, a few commenters recommended that the Commission require a fixed price at the commencement of an offering. *See, e.g.*, Joinvestor Letter; RocketHub Letter. We address those comments in Section II.B.6.

175 *See* Rule 201(l) of Regulation Crowdfunding.

methods used for determining the price, coupled with investors' rights to cancel their investment upon determination of the final price, provide sufficient opportunity for investors to evaluate the price.

(f) Ownership and Capital Structure

(i) Proposed Rules

Consistent with Section 4A(b)(1)(H), we proposed in Rule 201(m) of Regulation Crowdfunding to require an issuer to provide a description of its ownership and capital structure. This disclosure would include:

- the terms of the securities being offered and each other class of security of the issuer, including the number of securities being offered and those outstanding, whether or not such securities have voting rights, any limitations on such voting rights, how the terms of the securities being offered may be modified and a summary of the differences between such securities and each other class of security of the issuer, and how the rights of the securities being offered may be materially limited, diluted or qualified by the rights of any other class of security of the issuer;
- a description of how the exercise of the rights held by the principal shareholders of the issuer could affect the purchasers of the securities;
- the name and ownership level of persons who are 20 Percent Beneficial Owners;
- how the securities being offered are being valued, and examples of methods for how such securities may be valued by the issuer in the future, including during subsequent corporate actions;
- the risks to purchasers of the securities relating to minority ownership in the issuer and the risks associated with corporate actions including additional issuances of

securities, issuer repurchases of securities, a sale of the issuer or of assets of the issuer or transactions with related parties; and

- a description of the restrictions on the transfer of the securities.

As proposed, the rules would require disclosure of the number of securities being offered and those outstanding, whether or not such securities have voting rights, any limitations on such voting rights and a description of the restrictions on the transfer of the securities.

(ii) Comments on the Proposed Rules

A number of commenters supported the proposed ownership and capital structure disclosure rules,[176] while two commenters opposed them as burdensome.[177] One of these commenters suggested that issuers should only be required to disclose the price of a share and the percentage ownership represented by a share, and noted that the principals of an issuer conducting a crowdfunding offering may not consider the issuer's capital structure or whether its shareholders will have voting rights.[178]

(iii) Final Rules

We are adopting the ownership and capital structure disclosure rules as proposed, with the addition of language specifying that beneficial ownership must be calculated no earlier than 120 days prior to the date of the filing of the offering statement or report,[179] consistent with the treatment of beneficial ownership elsewhere in the rule.[180] Investors in crowdfunding transactions

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176 *See, e.g.*, CFA Institute Letter; Commonwealth of Massachusetts Letter; Hackers/Founders Letter; Joinvestor Letter; NASAA Letter; RocketHub (supporting only to the extent that such disclosures do not require additional form submission or accountant or legal work); Saunders Letter; Wilson Letter.

177 *See* Campbell R. Letter; Schatz Letter.

178 Schatz Letter.

179 *See* Rule 201(m) of Regulation Crowdfunding.

180 *See* Rule 201(c) of Regulation Crowdfunding.

will benefit from clear disclosure about the terms of the securities being offered and each other class of security of the issuer. The final rules require disclosure of the number of securities being offered and those outstanding, whether or not such securities have voting rights, any limitations on such voting rights[181] and a description of the restrictions on the transfer of securities.[182] Although Section 4A(b)(1)(H) does not specifically call for all aspects of this disclosure, we believe that such disclosure is necessary to provide investors with a more complete picture of the issuer's capital structure than would be obtained solely pursuant to the statutory requirements. This should help investors better evaluate the terms of the offer before making an investment decision.

(g) Additional Disclosure Requirements

(i) Proposed Rules

We also proposed to require the following additional disclosures:[183]

- disclosure of the name, SEC file number and Central Registration Depository number ("CRD number") (as applicable)[184] of the intermediary through which the offering is being conducted;
- disclosure of the amount of compensation paid to the intermediary for conducting the offering, including the amount of any referral or other fees associated with the offering;
- certain legends in the offering statement;
- disclosure of the current number of employees of the issuer;

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181 *Id.*

182 *See* Rule 501 of Regulation Crowdfunding and Section II.E.2 for a discussion of restrictions on resales.

183 Section 4A(b)(1)(I) provides us with discretion to require crowdfunding issuers to provide additional information for the protection of investors and in the public interest.

184 The Financial Industry Regulatory Authority, Inc. ("FINRA") issues CRD numbers to registered broker-dealers.

- a discussion of the material factors that make an investment in the issuer speculative or risky;
- a description of the material terms of any indebtedness of the issuer, including the amount, interest rate, maturity date and any other material terms;
- disclosure of any exempt offerings conducted within the past three years; and
- disclosure of related-party transactions since the beginning of the issuer's last fiscal year in excess of five percent of the aggregate amount of capital raised by the issuer in reliance on Section 4(a)(6) during the preceding 12-month period, inclusive of the amount the issuer seeks to raise in the current offering.

(ii) Comments on the Proposed Rules

Identity of the Intermediary. Several commenters supported the proposed requirement that issuers identify the intermediary through which the offering is being conducted.[185] Two commenters opposed such a requirement as unnecessary.[186]

Compensation Paid to the Intermediary. Some commenters supported the proposed requirement that issuers disclose the amount of compensation paid to the intermediary for conducting the offering, including the amount of any referral or other fees associated with the offering.[187] One commenter noted that to the extent components of the intermediary's fee are percentage based, the exact amount of the compensation may not be calculable at the onset of an

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185 *See, e.g.*, Commonwealth of Massachusetts Letter; Joinvestor Letter; Schwartz Letter; Wilson Letter (recommending that issuers also disclose whether the intermediary specializes in offerings based on criteria such as industry size or type).

186 *See* Public Startup Letter 2; RocketHub.

187 *See, e.g.*, ASSOB Letter; Commonwealth of Massachusetts Letter; RocketHub Letter; Startup Valley Letter; Wilson Letter. *But see, e.g.*, Grassi Letter (opposing the requirement unless offering proceeds will be used to compensate the intermediary); Public Startup Letter 2; Schwartz Letter.

offering.[188] A few commenters recommended that issuers also should disclose all payments and fees, if any, they make to the intermediary.[189]

Legends. Comments were mixed as to the proposed requirement that issuers include specified legends in the offering statement about the risks of investing in a crowdfunding transaction and the required ongoing reports. Some commenters supported such a requirement,[190] while others opposed the requirement.[191]

Current Number of Employees. While several commenters supported the proposed requirement that issuers disclose their current number of employees,[192] two commenters opposed such a requirement.[193] One commenter opposed this requirement, noting that the number of employees is not useful for investors in evaluating early-stage startups, and is likely to increase during the course of a crowdfunding offering conducted concurrently with an offering pursuant to Rule 506(c).[194] This commenter also noted that many early-stage startups spend the majority of their initial funds on consultants.[195] Another commenter noted that it may be unreasonably costly, relative to the benefit gained, to accurately count the number of employees in instances where

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188 *See* RocketHub Letter.

189 *See, e.g.*, ASSOB Letter (recommending disclosure of all payments); RocketHub Letter (recommending disclosure of fees paid for compliance and overhead to enhance transparency for investors).

190 *See, e.g.*, ABA Letter; CFA Institute Letter; Commonwealth of Massachusetts Letter; Jacobson Letter; Schwartz Letter; Wilson Letter.

191 *See, e.g.*, Grassi Letter (recommending that general risks be disclosed on the intermediaries' platforms rather than in each issuer's offering statement); Hackers/Founders Letter (noting that crowdfunding issuers will tend to be smaller and lack the resources of large companies, and intermediaries should be required to provide examples of risks associated with crowdfunding offerings); Public Startup Letter 2; Startup Valley Letter (stating that a legend by the issuer about the risks of investing in a crowdfunding transaction is not needed because it is the responsibility of the intermediary to educate the public about this information).

192 *See, e.g.*, NASAA Letter; Wilson Letter; Zhang Letter.

193 *See* Schwartz Letter; Wefunder Letter.

194 *See* Wefunder Letter.

195 *Id*.

businesses engage many contract workers, or have workers on arrangements such as "flex-time" or "half-time."[196]

Risk Factors. Commenters were divided as to the proposed requirement that issuers discuss the material factors that make an investment in the issuer speculative or risky. A number of commenters supported this proposed requirement,[197] while a number of others opposed it.[198] Some commenters recommended that we provide examples of, or develop standard disclosures for, issuer risk factor discussions.[199]

Indebtedness. Commenters supported the proposed requirement that issuers describe the material terms of any indebtedness of the issuer.[200] Two commenters recommended that we clarify that this disclosure requirement could be satisfied if the issuer includes such disclosure in its financial statements.[201] Another recommended that we require issuers to disclose the identities of their creditors.[202]

Prior Exempt Offerings. Commenters supported the proposed requirement that issuers disclose their prior exempt offerings.[203] One commenter recommended that we require additional

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196 *See* Schwartz Letter.

197 *See, e.g.*, ASSOB Letter; CFA Institute Letter; Commonwealth of Massachusetts Letter; Consumer Federation Letter; EMKF Letter; Jacobson Letter; McGladrey Letter; STA Letter; StartupValley Letter; Wilson Letter.

198 *See, e.g.*, ABA Letter; Campbell R. Letter; Cole A. Letter; Grassi Letter; Hackers/Founders Letter; RocketHub Letter (recommending that a generic 500-word statement suffice); Schwartz Letter; Scruggs Letter.

199 *See, e.g.*, Commonwealth of Massachusetts Letter; EMKF Letter; Heritage Letter (recommending also that the Commission define "material"); Jacobson Letter; SBA Office of Advocacy Letter. *But see*, StartupValley Letter (opposing such a recommendation).

200 *See, e.g.*, Consumer Federation Letter; ODS Letter; Schwartz Letter; Wilson Letter.

201 *See* Grassi Letter; EY Letter.

202 *See* ODS Letter.

203 *See, e.g.*, CFA Institute Letter (recommending a brief statement about prior capital raising transactions); Commonwealth of Massachusetts Letter; Grassi Letter; Joinvestor Letter; ODS Letter; Parsont Letter; RoC

disclosure to help non-accredited investors understand how well aligned their interests are with earlier accredited investors,[204] while other commenters suggested scaling back this disclosure in order to contain costs.[205]

Related-Party Transactions. Commenters generally supported our proposal to require disclosure of certain related-party transactions between the issuer and any director or officer of the issuer, any person who is a 20 Percent Beneficial Owner, any promoter of the issuer (if the issuer was incorporated or organized within the past three years) or immediate family members of the foregoing persons.[206] Rather than using the definition of "immediate family member" contained in Item 404 of Regulation S-K,[207] one commenter recommended that we use a common definition for "immediate family member" in the related-party transactions context and "member of the family of the purchaser or the equivalent" in the resale restrictions context.[208]

One commenter supported the proposal to limit the disclosure of related-party transactions to transactions since the beginning of the issuer's last fiscal year.[209] Other commenters recommended that the related-party transaction disclosure cover the period for which financial

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Letter (supporting the disclosure covering the past three years); RocketHub Letter (recommending disclosure of successful prior offerings only); Whitaker Chalk Letter (recommending that the disclosure exclude the target amount of any offerings made in reliance on Section 4(a)(6) and whether such target was reached); Wilson Letter. *But see, e.g.*, Heritage Letter; Public Startup Letter 2; Schwartz Letter; Wefunder Letter.

204 *See* Parsont Letter.

205 *See, e.g.*, Grassi Letter (recommending disclosure of only the date, amount raised, type of securities sold and a link to a website where more information on such prior offerings can be found); Wefunder Letter (recommending disclosure of only the aggregate capital raised in all prior exempt transactions, as well as the date, terms, valuation of and types of securities issued in the most recent exempt offering).

206 *See, e.g.*, AICPA Letter (recommending disclosure of transactions between the issuer and 10 percent beneficial owners); Commonwealth of Massachusetts Letter; Grassi Letter (also recommending disclosure of transactions between the issuer and employees or affiliated entities with common ownership or control); NASAA Letter; RocketHub Letter; Wilson Letter. *But see*, Public Startup Letter 2; Schwartz Letter.

207 17 CFR 229.404.

208 *See* Brown J. Letter. *See also*, Section II.E.2 for a discussion of the restrictions on resales.

209 *See* RocketHub Letter.

statements are required.[210] In addition, one commenter supported the proposal to limit disclosure of related-party transactions based on the size of the offering,[211] while a few commenters suggested alternatives to such proposal.[212]

Other Disclosures. Several commenters specifically recommended that we not require any additional disclosures.[213] One commenter pointed out that there was no "catch-all" clause requiring any other material information not specifically enumerated in Rule 201 of Regulation Crowdfunding.[214]

Other commenters recommended that we require issuers to disclose general information;[215] executive compensation;[216] zoning issues and issues with the Environmental Protection Agency or Food and Drug Administration;[217] a copy of their articles of incorporation;[218] the extent to which they are affected by market risk, material contracts, business

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210 *See* AICPA Letter; Grassi Letter.

211 *See* AICPA Letter.

212 *See, e.g.*, Grassi Letter (recommending disclosure of all related-party transactions not deemed *de minimis*); NASAA Letter (recommending a lower percentage threshold); RocketHub Letter (recommending a fixed threshold).

213 *See, e.g.*, ABA Letter; Public Startup Letter 2; RocketHub Letter; Schwartz Letter.

214 *See* CrowdCheck Letter 1.

215 *See, e.g.*, ODS Letter; STA Letter; Tiny Cat Letter. Such general information may include the issuer's contact information; agent for service; information about the manner in which ownership interests will be evidenced; who will be providing record keeping services; where records of ownership will be maintained; and/or statements that the issuer may not provide account statements and that investors will have the responsibility of monitoring their investments, communicating with the record keeper and updating their information with the record keeper.

216 *See, e.g.*, Arctic Island Letter 4; Denlinger Letter 1 (recommending disclosure of deferred compensation, stock options or warrants, contingent payments for services, shareholder and other related-party loans and contingent liabilities); Grassi Letter (recommending separate amounts for base salary, bonus and an "other" category for the three highest paid individuals and the number and type of equity instruments granted); NASAA Letter; RFPIA Letter (recommending inclusion of owners' compensation).

217 *See, e.g.*, Arctic Island Letter 4.

218 *See, e.g.*, Hackers/Founders Letter.

backlogs and the names of, and number of shares being sold by, existing shareholders;[219] and the credit history of the business and the business owners.[220]

As discussed in Section II.B.2 below in connection with ongoing annual reports, a number of commenters recommended ways to make it easier for investors to locate an issuer's annual reports.[221]

(iii) Final Rules

We are adopting the additional disclosure requirements as proposed in Rule 201 with several modifications. As discussed below, we have added a requirement to disclose any material information necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading.[222] We also have modified the rule to require disclosure of the compensation to be paid to the intermediary so that it could be disclosed either as a dollar amount or percentage of the offering amount or as a good faith estimate if the exact amount is not available at the time of the filing.[223] We also have added a requirement to disclose the location on the issuer's website where investors will be able to find the issuer's annual report and the date by which such report will be available on the issuer's website.[224] In addition, we have added a requirement to disclose whether the issuer or any of its predecessors previously has failed to comply with the ongoing reporting requirements of Regulation Crowdfunding.[225]

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219 *See, e.g.*, CFA Institute Letter.

220 *See, e.g.*, SBM Letter.

221 *See, e.g.*, Arctic Island Letter 5; CFA Institute Letter (recommending advance notice as to when and where annual reports will be available); RocketHub Letter.

222 *See* Rule 201(y) of Regulation Crowdfunding.

223 See Rule 201(o) of Regulation Crowdfunding.

224 *See* Rule 201(w) of Regulation Crowdfunding.

225 *See* Rule 201(x) of Regulation Crowdfunding.

We agree with the suggestion by some commenters that issuers should not be required to disclose in multiple places the information required to be provided to investors.[226] As a result, to avoid duplicative disclosure, an issuer will not be required to repeat what is already provided elsewhere in the issuer's disclosure, including the financial statements.[227] Issuers may cross-reference within the offering statement or report, including to the location of the information in the financial statements. [228]

Identity of the Intermediary. Despite the suggestion of one commenter that this disclosure is unnecessary,[229] we believe requiring an issuer to identify the name, SEC file number and CRD number (as applicable) of the intermediary through which the offering is being conducted should assist investors and regulators in obtaining information about the offering and use of the exemption.[230] It also could help investors obtain background information on the intermediary, for instance, through filings made by the intermediary with the Commission, as well as through the Financial Industry Regulatory Authority's ("FINRA") BrokerCheck system for broker-dealers[231] or a similar system, if created, for funding portals.

Compensation Paid to the Intermediary. Requiring an issuer to disclose the amount of compensation paid to the intermediary for conducting the offering, including the amount of any referral or other fees associated with the offering, will permit investors and regulators to determine how much of the proceeds of the offering is used to compensate the intermediary.

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226 *See, e.g.*, EY Letter (noting that certain required disclosure would be included in an issuer's financial statements); Grassi Letter (same).

227 *See* Instruction to Item 201 of Regulation Crowdfunding.

228 *Id*.

229 *See* RocketHub Letter.

230 *See* Rule 201(n) of Regulation Crowdfunding.

231 *See* FINRA, FINRA BrokerCheck, *available at* http://www.finra.org/Investors/ToolsCalculators/BrokerCheck/P015175.

Based on a comment received,[232] we understand that in some instances the exact amount of compensation and fees to be paid to the intermediary will not be known at the time the Form C is filed, and we have modified the rule from the proposal to address this issue. Consistent with this understanding, and to avoid suggesting that only amounts certain and paid to date must be disclosed, the final rules require disclosure of all compensation paid or to be paid to the intermediary for conducting the offering, which may be disclosed as a dollar amount or as a percentage of the offering amount. If the exact amount of the compensation paid or to be paid is not available at the time of the filing, issuers are permitted to provide a good faith estimate.[233]

In addition, we are modifying the rule text from the proposal to require issuers to disclose any other direct or indirect interest in the issuer held by the intermediary, or any arrangement for the intermediary to acquire such an interest.[234] The proposed rules would have prohibited an intermediary from holding any financial interest in the issuers conducting offerings on its platforms. However, as discussed in Section II.C.2.b below, the final rules permit intermediaries to hold such interests. We believe that, similar to the amount of compensation paid to the intermediary, an intermediary's interests in an issuer and the issuer's transaction could be material to an investment decision in the issuer. Therefore, we believe that issuers should disclose such interests to investors.

Legends. We are adopting this requirement as proposed.[235] The requirement for an issuer to include in the offering statement specified legends about the risks of investing in a crowdfunding transaction is intended to help investors understand the general risks of investing in

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232 *See* RocketHub Letter.

233 *See* Rule 201(o)(1) of Regulation Crowdfunding.

234 *See* Rule 201(o)(2) of Regulation Crowdfunding.

235 *See* Item 2 of General Instruction III to Form C.

a crowdfunding transaction. We continue to believe, despite the suggestions of some commenters,[236] that requiring legends in each issuer's offering statement, regardless of any general warnings available on an intermediary's platform, will provide additional investor protection with minimal costs. For example, the requirement that an issuer include in the offering statement certain legends about the required ongoing reports, including how those reports will be made available to investors and how an issuer may terminate its ongoing reporting obligations, will help investors understand an issuer's ongoing reporting obligations and how they will be able to access those reports.

Current Number of Employees. Consistent with the proposal and the recommendation of several commenters,[237] the final rules require disclosure of the current number of employees.[238] We believe this disclosure is important to investors in evaluating a crowdfunding transaction because it will give investors a sense of the size of the issuers using the exemption. We expect that the early-stage issuers who are likely to use securities-based crowdfunding will not have many employees, so we do not believe this requirement will be unreasonably burdensome.

Risk Factors. We are adopting this disclosure requirement as proposed.[239] While some commenters expressed concerns about potential expenses or confusion associated with risk disclosure,[240] we agree with those commenters who indicated that disclosure of the material factors that make an investment in the issuer speculative or risky is important to help investors

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236 *See, e.g.*, Grassi Letter; Hackers/Founders Letter; Public Startup Letter 2; Startup Valley Letter.

237 *See, e.g.*, NASAA Letter; Wilson Letter; Zhang Letter.

238 *See* Rule 201(e) of Regulation Crowdfunding.

239 *See* Rule 201(f) of Regulation Crowdfunding.

240 *See, e.g.*, Campbell R. Letter; Cole A. Letter; Grassi Letter; Hackers/Founders Letter; RocketHub Letter; Schwartz Letter; Scruggs Letter.

understand the risks of investing in a specific issuer's offering.[241] To help investors to better understand these risks, we believe that risk factor disclosure should be tailored to the issuer's business and the offering and should not repeat the factors addressed in the required legends.[242] For similar reasons, we are not providing examples of, or developing standard disclosure for, issuer risk factor discussions, as we believe issuers will be in the best positions to articulate the risks associated with their business and offerings in light of their particular facts and circumstances.

Indebtedness. Consistent with the proposal, we are adopting the requirement to provide a description of the material terms of any indebtedness of the issuer.[243] We believe disclosure of the material terms of any indebtedness of the issuer, including, among other items, the amount, interest rate and maturity date of the indebtedness, is important to investors because servicing debt could place additional pressures on an issuer in the early stages of development. We expect that for many issuers this information will be included in the financial statements, which will satisfy this reporting requirement.[244]

While one commenter recommended that we require issuers to disclose the identities of their creditors,[245] we do not believe, as a general matter, that such disclosure would provide

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241 *See, e.g.*, ASSOB Letter; CFA Institute Letter; Commonwealth of Massachusetts Letter; Consumer Federation Letter; EMKF Letter; Jacobson Letter; McGladrey Letter; STA Letter; StartupValley Letter; Wilson Letter.

242 *See* Item 2 of General Instruction III to Form C.

243 *See* Rule 201(p) of Regulation Crowdfunding.

244 *See* Instruction to Rule 201 of Regulation Crowdfunding; Items 1 and 3 of General Instruction III to Form C.

245 *See* ODS Letter.

meaningful information to investors. Accordingly, under the final rules, such disclosure is required only to the extent the creditor's identity is a material aspect of the indebtedness.[246]

Prior Exempt Offerings. Consistent with the proposal and with commenters' recommendations, we are requiring issuers to provide disclosure about the exempt offerings that they conducted within the past three years.[247] For each exempt offering within the past three years, issuers must describe the date of the offering, the offering exemption relied upon, the type of securities offered and the amount of securities sold and the use of proceeds.[248] We believe that information about prior offerings will better inform investors about the capital structure of the issuer and will provide information about how prior offerings were valued.

Related-Party Transactions. We are adopting this disclosure requirement substantially as proposed.[249] Related-party transactions create potential conflicts of interest that may result in actions that benefit the related parties at the expense of the issuer or the investors. After considering the comments received, we continue to believe the related-party transactions disclosure will assist investors in obtaining a more complete picture of the financial relationships between certain related parties and the issuer and provide additional insight as to potential uses of the issuer's resources, including the proceeds of the offering. The final rule differs from the proposal in that an issuer is required to disclose transactions with any person who is, as of the most recent practicable date but no earlier than 120 days prior to the date the offering statement or report is filed, the beneficial owner of 20 percent or more of the issuer's outstanding voting equity securities. Limiting the relevant period to 120 days prior to the date of the offering statement or

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246 *See* Rule 201(y) of Regulation Crowdfunding.

247 *See* Rule 201(q) of Regulation Crowdfunding.

248 *See* Instruction to paragraph (q) of Rule 201 of Regulation Crowdfunding.

249 *See* Rule 201(r) of Regulation Crowdfunding.

report is consistent with the treatment of beneficial ownership elsewhere in Regulation Crowdfunding.[250] We also believe this limitation and the consistency it provides will help limit compliance costs for issuers.

The final rule also includes an instruction to clarify that, for purposes of Rule 201(r), a transaction includes, but is not limited to, any financial transaction, arrangement or relationship (including any indebtedness or guarantee of indebtedness) or any series of similar transactions, arrangements or relationships.[251] This instruction is consistent with Item 404 of Regulation S-K.[252]

Given the early stage of development of the small businesses and startups that we expect will seek to raise capital pursuant to Section 4(a)(6), as well as the investment limits prescribed by the rules, we believe that limiting the disclosure of related-party transactions to transactions occurring since the beginning of the issuer's last fiscal year, as proposed, will help to limit compliance costs for issuers while still providing investors with sufficient information to evaluate the relationship between related parties and the issuer.[253] In addition, we are requiring issuers to disclose only related-party transactions that, in the aggregate, are in excess of five percent of the aggregate amount of capital raised by the issuer in reliance on Section 4(a)(6) during the preceding 12-month period, inclusive of the amount the issuer seeks to raise in the current offering under Section 4(a)(6). We also have added an instruction to clarify that any series of similar transactions, arrangements or relationships should be aggregated for purposes of determining

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250 *See, e.g.*, Rules 201(c) and 201(m) of Regulation Crowdfunding.

251 *See* Instruction 2 to Rule 201(r) of Regulation Crowdfunding.

252 *See* Instruction 2 to Item 404(a) of Regulation S-K [17 CFR 229.404(a)].

253 We note, however, that financial statements covering the two most recently completed fiscal years will include disclosure of related-party transactions, as required by U.S. GAAP, for each of the years presented.

whether related-party transactions should be disclosed.[254] For example, an issuer seeking to raise $1 million will be required to disclose related-party transactions that, in the aggregate, are in excess of $50,000, which is the same dollar threshold required in Form 1-A[255] for offerings of any size made pursuant to Tier 1 of Regulation A,[256] and an issuer that raises $250,000 will be required to disclose such transactions in excess of $12,500. We believe that, in light of the sizes and varieties of issuers that may make offerings in reliance on Section 4(a)(6), this approach could mitigate the potential for the requirement to be disproportionate to the size of certain offerings and issuers. While one commenter suggested we use a percentage threshold less than five percent, we believe this threshold appropriately takes into consideration the need to provide investors with relevant information about the issuer's activities involving related parties during this crucial early stage of development.

As suggested by one commenter,[257] in a change from the proposal, we are adopting a definition for "member of the family" in the related-party transactions context that is consistent with the definition of "member of the family of the purchaser or the equivalent" in the resale restrictions context.[258] The final rule defines "member of the family" as a "child, stepchild, grandchild, parent, stepparent, grandparent, spouse or spousal equivalent, sibling, mother-in-law, father-in-law, son-in-law, daughter-in-law, brother-in-law, or sister-in-law, [including] adoptive relationships" of any of the persons identified in Rules 201(r)(1), (r)(2) or (r)(3).[259] This

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254 *See* Instruction 1 to Rule 201(r) of Regulation Crowdfunding.

255 17 CFR 239.900

256 17 CFR 230.251 through 230.263

257 *See* Brown J. Letter.

258 *See* Rule 501(a) of Regulation Crowdfunding;

259 *See* Rule 201(r)(4) of Regulation Crowdfunding.

definition tracks the definition of "immediate family" in Exchange Act Rule 16a-1(e),[260] but with the addition of "spousal equivalent," which the final rule defines to mean "a cohabitant occupying a relationship generally equivalent to that of a spouse."[261] We believe a common definition of "member of the family" that is consistent with our disclosure rules in other contexts[262] will provide certainty for issuers in identifying the persons covered by the rule.

Other Disclosures. We are adopting this provision as proposed but with the addition of three issuer disclosure requirements in response to comments received.

The first is a requirement that an issuer disclose the location on its website where investors will be able to find the issuer's annual report and the date by which such report will be available on its website.[263] We believe this requirement addresses the concern expressed by commenters that investors may not know where to find an issuer's annual report. We do not believe physical delivery of the annual report is necessary due to the electronic nature of the crowdfunding marketplace, nor do we believe that e-mail delivery of the annual report is practical because the issuer may not have access to e-mail addresses of its investors. Instead, we are requiring issuers to disclose this information in the offering statement, which will assist investors in locating the information while limiting the compliance costs for issuers.

The second additional disclosure requirement, as suggested by a commenter,[264] is a requirement that the disclosure include any material information necessary in order to make the

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260 17 CFR 240.16a-1(e).

261 *See* Rule 201(r)(4) of Regulation Crowdfunding.

262 *See*, *e.g.*, Exchange Act Rule 16a-1(e).

263 *See* Rule 201(w) of Regulation Crowdfunding. *See also,* Section II.B.2 for a discussion of the requirement on issuers to post their annual reports on their websites.

264 *See* CrowdCheck Letter 1.

statements made, in light of the circumstances under which they were made, not misleading.[265] This provision should help ensure that investors have all of the material information they need on which to base their investment decisions.

The third additional requirement, similar to suggestions from some commenters,[266] requires the issuer to disclose whether it or any of its predecessors previously failed to comply with the ongoing reporting requirements of Regulation Crowdfunding.[267] While we continue to believe, and the final rules provide, that only those issuers that have failed to file their two most recent annual reports should be prohibited from relying on the exemption available under Section 4A(6), we also believe that any history of non-compliance with ongoing reporting obligations would provide important information to investors about the issuer.

Although we appreciate that commenters made various suggestions for additional issuer disclosure requirements, such as those relating to executive compensation, market risk and material contracts, we are not mandating further disclosures. In adopting issuer requirements for Regulation Crowdfunding, we have been mindful of the limited resources and start-up operations of issuers likely to use security-based crowdfunding and have sought to consider the need to provide investors with relevant information to make an informed investment decision while limiting the compliance costs for issuers. We believe the issuer disclosure requirements we are adopting along with other protections, such as investment limits, achieve this goal.

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265 *See* Rule 201(y) of Regulation Crowdfunding.

266 *See* Grassi Letter; RocketHub Letter.

267 *See* Rule 201(x) of Regulation Crowdfunding.

(2) Financial Disclosure

Section 4A(b)(1)(D) requires "a description of the financial condition of the issuer." It also establishes a framework of tiered financial disclosure requirements based on aggregate target offering amounts of the offering and all other offerings made in reliance on Section 4(a)(6) within the preceding 12-month period.

(a) Financial Condition Discussion

(i) Proposed Rules

Consistent with Section 4A(b)(1)(D), we proposed in Rule 201(s) of Regulation Crowdfunding to require an issuer to provide a narrative discussion of its financial condition.

(ii) Comments on the Proposed Rules

Commenters generally supported the proposed requirement that issuers provide a narrative discussion of their financial condition.[268] One commenter expressed concern that the requirement could be challenging for issuers at an early stage of development and result in duplicative disclosure.[269] The same commenter suggested that issuers be encouraged, rather than mandated, to discuss material historical operating results.[270]

(iii) Final Rules

We are adopting this requirement as proposed, with a few technical modifications.[271] Rule 201(s) clarifies that the description must include, to the extent material, a discussion of liquidity, capital resources and historical results of operations. Rule 201(s) also includes an

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268 *See, e.g.*, ABA Letter; CFA Institute Letter; CFIRA Letter 5; Commonwealth of Massachusetts Letter; Grassi Letter; Jacobson Letter; Joinvestor Letter; Saunders Letter. *But see, e.g.*, EY Letter; Public Startup Letter 2; RocketHub Letter.

269 *See* EY Letter.

270 *Id*.

271 *See* Rule 201(s) of Regulation Crowdfunding.

instruction noting that issuers will be required to include a discussion of each period for which financial statements are provided and a discussion of any material changes or trends known to management in the financial condition and results of operations of the issuer subsequent to the period for which financial statements are provided.[272] In connection with this instruction, an issuer will need to consider whether more recent financial information is necessary to make the disclosure in the offering document not misleading. The instruction in final Rule 201(s) was included in proposed Rule 201(t) as an instruction to the financial statement requirements, but we have moved this instruction to Rule 201(s) because it elicits narrative disclosure that we believe is more appropriately presented as part of the discussion of the issuer's financial condition. In addition, another instruction clarifies that references to the issuer in Rule 201(s) refer to the issuer and its predecessors, if any.[273]

We expect that the discussion required by the final rule and instructions will inform investors about the financial condition and results of operations of the issuer by providing management's perspective on the issuer's operations and financial results, including information about the issuer's liquidity and capital resources and any known trends or uncertainties that could materially affect the company's results. Because issuers seeking to engage in crowdfunding transactions will likely be smaller, less complex and at an earlier stage of development than issuers conducting registered offerings or Exchange Act reporting companies, we expect that the discussion generally will not, contrary to the concern of at least one commenter,[274] need to be as lengthy or detailed as the management's discussion and analysis of financial condition and results

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272 *See* Instruction 1 to Rule 201(s) of Regulation Crowdfunding.

273 *See* Instruction 4 to Rule 201(s) of Regulation Crowdfunding.

274 *See* EY Letter.

of operations of those issuers. Accordingly, we are not prescribing a specific content or format for this information, but instead set forth general principles for making this disclosure.[275] The discussion should address, to the extent material, the issuer's historical results of operations in addition to its liquidity and capital resources. If an issuer does not have a prior operating history, the discussion should focus on financial milestones and operational, liquidity and other challenges. If an issuer has a prior operating history, the discussion should focus on whether historical earnings and cash flows are representative of what investors should expect in the future. An issuer's discussion of its financial condition should take into account the proceeds of the offering and any other known or pending sources of capital. Issuers also should discuss how the proceeds from the offering will affect their liquidity, whether these funds and any other additional funds are necessary to the viability of the business and how quickly the issuer anticipates using its available cash. In addition, issuers should describe the other available sources of capital to the business, such as lines of credit or required contributions by principal shareholders. To the extent these items of disclosure overlap with the issuer's discussion of its business or business plan, issuers are not required to make duplicate disclosures.[276] While we are not mandating a specific presentation, we expect issuers to present the required disclosures, including any other information that is material to an investor, in a clear and understandable manner.

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[275] *See* Instructions 1 and 2 to Rule 201(s) of Regulation Crowdfunding.

[276] *See* Instruction to Rule 201 of Regulation Crowdfunding.

(b) Financial Disclosures

(i) Proposed Rules

Proposed Rule 201(t) of Regulation Crowdfunding would have established financial statement disclosure requirements that are based on aggregate target offering amounts within the preceding 12-month period:

- issuers offering $100,000 or less would be required to file with the Commission and provide to investors and the relevant intermediary income tax returns filed by the issuer for the most recently completed year (if any) and financial statements that are certified by the principal executive officer to be true and complete in all material respects;
- issuers offering more than $100,000, but not more than $500,000, would be required to file with the Commission and provide to investors and the relevant intermediary financial statements reviewed by a public accountant that is independent of the issuer; and
- issuers offering more than $500,000 would be required to file with the Commission and provide to investors and the relevant intermediary financial statements audited by a public accountant that is independent of the issuer.

Under proposed Rule 201(t), issuers would be permitted to voluntarily provide financial statements that meet the requirements for a higher aggregate target offering amount.

The proposed rules also would have set forth the following requirements for the financial statements:

- Basis of Accounting. All issuers would be required to file with the Commission and provide to investors and the relevant intermediary a complete set of their financial statements (balance sheets, income statements, statements of cash flows and statements of

changes in owners' equity), prepared in accordance with U.S. generally accepted accounting principles ("U.S. GAAP").

- Public Accountant Requirements. To qualify as independent of the issuer, a public accountant would be required to comply with the Commission's independence rules, which are set forth in Rule 2-01 of Regulation S-X.[277]
- Periods Covered in the Financial Statements. The financial statements would be required to cover the shorter of the two most recently completed fiscal years or the period since inception of the business.
- Age of Financial Statements. During the first 120 days of the issuer's fiscal year, an issuer would be able to conduct an offering in reliance on Section 4(a)(6) and the related rules using financial statements for the fiscal year prior to the most recently completed fiscal year if the financial statements for the most recently completed fiscal year are not otherwise available or required to be filed.
- Review and Audit Standards. Reviewed financial statements would be required to be reviewed in accordance with the Statements on Standards for Accounting and Review Services ("SSARS") issued by the American Institute of Certified Public Accountants ("AICPA"). Audited financial statements would be required to be audited in accordance with the auditing standards issued by either the AICPA or the Public Company Accounting Oversight Board ("PCAOB").
- Review and Audit Reports. Issuers would be required to file with the Commission and provide to investors and the relevant intermediary a copy of the public accountant's review

[277] 17 CFR 210.2-01.

or audit report. An issuer that received an adverse opinion or disclaimer of opinion in its audit report would not be in compliance with the audited financial statement requirements.

- Exemptions from the Financial Statement Requirements. The proposed rules would not exempt any issuers from the financial statement requirements.

(ii) Comments on the Proposed Rules

Commenters were divided on the proposed financial statement requirements,[278] although commenters generally supported allowing issuers to voluntarily provide financial statements that meet the requirements for a higher aggregate target offering amount.[279]

Offerings of $100,000 or less. In general, commenters supported requiring issuers to provide financial statements certified by the principal executive officer to be true and complete in all material respects.[280] Further, several recommended that all issuers relying on the Section 4(a)(6) exemption be required to provide such certification.[281]

Commenters were divided on the requirement that issuers offering $100,000 or less file and provide to investors their federal income tax returns. Supporters of the tax return requirement noted that income tax returns would be a source of credible information for investors that should be readily available without requiring issuers to bear significant additional preparation

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278 For an example of those who generally supported the proposed financial disclosure requirements, *see, e.g.*, ABA Letter (recommending some modifications); CFA Institute Letter; Commonwealth of Massachusetts Letter; Consumer Federation Letter (the financial information is critical to an informed evaluation of the investment opportunity); Denlinger Letter 1; Funderbuddies Letter; NASAA Letter.

For an example of those who generally opposed, *see, e.g.*, AEO Letter; Joinvestor Letter (recommending that only issuer-generated documents produced in good faith be required); Marsala Letter; RocketHub (stating that "requirements are excessive in cost and misguided in intent"); Traklight Letter (recommending that instead of pre-raise and ongoing financial statement reviews or audits, issuers only be required to have a limited review engagement on the use of proceeds after the raise); Zhang Letter.

279 *See, e.g.*, AICPA Letter; Denlinger Letter 1; Grassi Letter; Heritage Letter; RocketHub Letter; Wilson Letter. *But see* Public Startup Letter 2.

280 *See, e.g.*, AICPA Letter; Zeman Letter.

281 *See, e.g.*, AICPA Letter; Denlinger Letter 1; Grassi Letter; Jacobson Letter. *But see* Public Startup Letter 2.

expenses.[282] On the other hand, opponents of the tax return requirement raised concerns about privacy,[283] identity theft and tax fraud.[284] One commenter expressed concern that small issuers may not be adequately prepared to consider the patchwork of state and federal privacy laws that might apply to the disclosure of tax returns.[285]

Several commenters suggested approaches to allow access by investors to the information available from a tax return,[286] including permitting issuers to digitally submit the data from their tax return in a standardized format.[287] Supporters of digital submission suggested that approach would provide a standardized format and protect issuers from accidental disclosure of confidential information. Commenters generally supported the proposal to require issuers to redact personally identifiable information from their tax returns,[288] although some requested clarifications.[289]

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282 *See, e.g.*, Angel Letter 1 ("tax returns are even more credible than audited financial statements, as companies are highly unlikely to exaggerate profitability to the IRS."); Fund Democracy Letter; NPCM Letter; Zeman Letter ("the small risk for these investors does not meet the consideration of audited financial statements.").

283 *See, e.g.*, AICPA Letter (disclosing an issuer's tax return "…has the potential to cause serious problems. Tax returns are intended to be confidential and should remain so."); Public Startup Letter 2; RocketHub Letter; SBM Letter; Wilson Letter (personal income tax information should be on a voluntary basis only); Zhang Letter.

284 *See* AICPA Letter.

285 *See* AICPA Letter.

286 *See, e.g.*, Arctic Island Letter 5 (recommending that only the two primary pages and not the schedules be made public); CrowdBouncer Letter (recommending the Commission allow issuers to disclose electronic transcripts of filed tax returns to investors through the intermediary platforms); NPCM (expressing concern that unless tax returns are filed as a PDF stamped by the IRS, there is no way to know if the posted document is a true reflection of the tax return); RocketHub Letter.

287 *See, e.g.*, RocketHub Letter (suggesting digital submission "will protect the issuers from accidental disclosure of confidential information, and will allow investors to view the information in a structured and consistent manner. For example, if each issuer were to upload their version of a financial statement, the responsibility of learning to understand each format would fall to the investor. Standardized formats for financial projections, financial statements, and business plans will allow investors to quickly compare issuances and more readily evaluate investment opportunities."); Zhang Letter.

288 *See, e.g.*, ABA Letter; AICPA Letter; Fund Democracy Letter; Whitaker Chalk Letter.

289 *See, e.g.*, ABA Letter (recommending the Commission provide a non-exhaustive list of the specific types of information that may be redacted); AICPA Letter (recommending that if the tax return requirement is adopted, the Commission define "personally identifiable information" and clarify that the redaction includes third-party information).

Two commenters recommended that the timing of financial statement disclosures correspond to any extended tax filing deadlines,[290] while two other commenters opposed such application.[291] Further, a few commenters supported the proposal to permit an issuer that has not yet filed its tax return for the most recently completed fiscal year to use the tax return filed for the prior year and update the information after filing the tax return for the most recently completed fiscal year.[292] One commenter recommended that at least one tax return be available,[293] and another recommended that the Commission provide guidance for issuers who have not filed a U.S. tax return.[294] One commenter supported requiring issuers to describe any material changes that are expected in the tax returns for the most recently completed fiscal year,[295] while another recommended that such disclosure be permitted, but not required.[296]

A number of commenters recommended raising the maximum offering amount for issuers that provide this level of financial information.[297]

Offerings of more than $100,000 but not more than $500,000. Some commenters supported the requirement in the proposed rules that offerings of more than $100,000 but not more

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290 *See* EY Letter; Grassi Letter.

291 *See, e.g.*, ASSOB Letter (recommending that issuers should provide their tax accounts within three months of the end of the reporting period); Fund Democracy Letter.

292 *See, e.g.*, Grassi Letter; RocketHub Letter.

293 *See* Fund Democracy Letter.

294 *See* AICPA Letter.

295 *See* Grassi Letter.

296 *See* RocketHub Letter (also recommending that the Commission define what qualifies as a material change).

297 *See, e.g.*, Hackers/Founders Letter ($500,000); Kickstarter Coaching Letter ($250,000); RocketHub Letter ($500,000); Zeman Letter (recommending that offerings under $500,000 require two years of tax returns and unaudited balance sheets).

than $500,000 include financial statements reviewed by an independent public accountant,[298] while other commenters opposed such requirement.[299] A number of commenters recommended a different range of offering amounts or methods for determining when an issuer is required to file and provide reviewed financial statements.[300]

Offerings of more than $500,000. We received extensive comments on our proposal that issuers offering more than $500,000 be required to file with the Commission and provide to investors and the relevant intermediary financial statements audited by an independent public accountant. A significant number of those commenters opposed the proposed requirement,[301] although some commenters expressed support.[302] Some commenters recommended the elimination of the audit requirement,[303] and others recommended that we consider additional criteria for determining when an issuer would be required to provide audited financial

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298 *See, e.g.*, Denlinger Letter 1; Leverage PR Letter (stating that the industry will evolve to provide lower cost reviews); StartEngine Letter 1 (stating that the industry will evolve to provide lower cost reviews, such as in the $1,500-$10,000 range for smaller, newer companies).

299 *See, e.g.*, Angel Letter 1 (recommending requiring audited financial statements if they are available and tax returns if they are not); Arctic Island Letter 5 (recommending only for issuers that have greater than $15 million in annual revenue); Johnston Letter; McGladrey Letter (recommending only after the issuer meets certain revenue and operational thresholds); NACVA Letter; Public Startup Letter 2; Zeman Letter.

300 *See, e.g.*, ABA Letter; CIFRA Letter 5 (noting the financial disclosure standards of the SBA's Section 8(a) program require reviewed financial statements for companies with gross annual receipts for $2 million to $10 million); Grassi Letter ($300,000 to $700,000); Kickstarter Coaching Letter ($250,000 to $1 million).

301 *See, e.g.*, AEO Letter; Angel Letter 1; AWBC Letter; CFIRA Letter 5; CfPA Letter; CrowdFundConnect Letter; EarlyShares Letter; EMKF Letter; EY Letter; Finkelstein Letter; FundHub Letter 1; Generation Enterprise Letter; Fryer Letter; Grassi Letter; Graves Letter; Guzik Letter 1; Hakanson Letter; Holland Letter; Johnston Letter; Kickstarter Coaching Letter; McGladrey Letter; Milken Institute Letter; NACVA Letter; NFIB Letter; NPCM Letter; NSBA Letter; PBA Letter; Reed Letter; RocketHub Letter; Saunders Letter; SBA Office of Advocacy Letter; SBEC Letter; SBM Letter; Seyfarth Letter; WealthForge Letter; Wefunder Letter; Woods Letter; Zeman Letter.

302 *See, e.g.*, AICPA Letter; Consumer Federation Letter; CSTTC Letter; Denlinger Letter 2; FundDemocracy Letter; Leverage PR; NASAA Letter; StartEngine Letter 1.

303 *See, e.g.*, CrowdFundConnect Letter; FundHub Letter 1; Johnston Letter; SBEC Letter; StartupValley Letter (for issuers less than two years old); Woods Letter.

statements.[304] A number of commenters opposed the proposed $500,000 threshold as being too low,[305] and a number recommended alternative thresholds.[306] A number of commenters stated that funding the upfront cost of an audit would be particularly difficult for issuers raising capital for the first time.[307]

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304 *See, e.g.*, Angel Letter 1 (only if such financial statements are available); Arctic Island Letter 5 (only apply to issuers that have greater than $15 million in revenue); EY Letter (only if issuer has raised $5 million in equity securities in crowdfunding transactions unless audited financial statements are otherwise available); McGladrey Letter (eliminate the audit requirements until the issuer meets certain revenue and operational thresholds); Reed Letter (if an audit is required, the requirement only apply to issuers that reach a certain size in investment or investors); RocketHub Letter ($5 million offering amount and the issuer has been in operation for more than two years). *But see* AICPA Letter (additional criteria would add complexity without any additional benefit).

305 *See, e.g.*, ABA Letter; CCA Letter; CFIRA Letter 5; CfPA Letter; CrowdFundConnect Letter; EarlyShares Letter; EMKF Letter; EY Letter; FundHub Letter 1; Generation Enterprise Letter; Grassi Letter; Graves Letter; Guzik Letter 1; Kickstarter Coaching Letter; Milken Institute Letter; NFIB Letter; PBA Letter; RocketHub Letter; SBA Office of Advocacy Letter; SBM Letter; Seyfarth Letter; WealthForge Letter; Wefunder Letter; Woods Letter. *But see* AICPA Letter; Denlinger Letter 1; Fund Democracy Letter; Zeman Letter.

306 *See, e.g.*, ABA Letter ($750,000); EarlyShares Letter ($1 million); EMKF Letter ($800,000); EY Letter ($5 million, unless audited financial statements are otherwise available); Grassi Letter ($700,000); Graves Letter ($900,000); Guzik Letter 1 ($700,000); Kickstarter Coaching Letter ($1 million); PBA Letter ($1 million); RocketHub Letter ($5 million and the issuer has been in operation for more than two years); Seyfarth Letter ($1 million); WealthForge Letter ($1 million).

307 *See, e.g.*, AEO Letter (expressing concern that start-up businesses with no revenue to date, and raising capital for the first time, would find it difficult or impossible to fund the cost of an audit); AWBC Letter; CFIRA Letter 5 (stating that the proposed level of financial disclosure for capital raises over $500,000 would be an impediment for small business when many will have limited financial resources to absorb the expense prior to raising capital using crowdfunding); CfPA Letter (suggesting the Commission determine an alternate audit threshold because "the costs of an audit must necessarily be incurred prior to an offering, and in the numerous expected cases of unsuccessful offerings, would lead to substantial net losses to the businesses that Crowdfunding is supposed to help"); EMKF Letter (stating that many of the issuers looking to raise capital through crowdfunding will be startups with little or no revenue to afford audited financial statements); Generation Enterprise Letter; Grassi Letter; Graves Letter; Holland Letter; McGladrey Letter; NSBA Letter; Reed Letter (noting that few start-ups could afford auditing fees); RocketHub Letter (stating that the filing and audit requirements establish an upfront cost that is too high for small businesses to accept); SBM Letter (noting that many startups do not have the resources to obtain audited financials); Seyfarth Letter (stating that the audit requirement will deny access to issuers who do not have the necessary upfront capital); WealthForge Letter; Wefunder Letter.

We received a number of comments expressing concern about the anticipated costs associated with audited financial statements.[308] Other commenters noted that costs would be lower than those estimated in the Proposing Release or in other comment letters.[309]

Basis of Accounting. Commenters generally were divided on whether issuers relying on Section 4(a)(6) should be required to prepare financial statements in accordance with U.S. GAAP.[310] Commenters in support of requiring U.S. GAAP noted the benefit to investors of

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308 *See, e.g.*, AEO Letter; CfPA Letter; CFIRA Letter 5; CrowdCheck Letter 4; ErrandRunner Letter; Finkelstein Letter; FundHub Letter 1 (stating that the difference in cost for reviewed versus audited financial statements could easily run into tens of thousands of dollars); Graves Letter (stating that a partner from a leading accounting firm predicted the cost to small businesses of providing audited financial statements could be upwards of $18,000 to $25,000); Grassi Letter (stating that audits take more time than companies seeking capital may have); NFIB Letter; RocketHub Letter; SBA Office of Advocacy Letter; SBEC Letter; SBM Letter; Seyfarth Letter; StartupValley Letter (stating that audits for small startups with no financials can cost $10,000 and that GAAP audits typically cost 25-50% more than other comprehensive basis of accounting audits); Stephenson Letter; Traklight Letter (stating that audit costs have been cited as low as $5,000 and as high as $20,000 for a startup; also stating that review costs are estimated at about 60% of the cost of an audit); WealthForge Letter.

309 *See, e.g.*, CCA Letter (analyzing regulatory costs borne by Title II issuers); CrowdFranchise Letter 1; CrowdFunding Network (stating that projected costs are already decreasing through market forces); D'Amore Letter; ddb*mckennon* Letter (noting that the majority of issuers will be newly formed with limited historical operations and that an audit for such companies may range from $4,000-$9,000 in year one); Denlinger Letter 1 (citing a study that found that about half of the cost of an audit is made up for in interest rate savings on bank loans); Denlinger Letter 2 (the market will evolve for small issuers such that audit costs may be in the range of $2,000-$4,000); FundHub Letter 2 (noting the emergence of CPA firms willing to do a complete audit for a startup business for $2,500 or less); Holm Letter (stating that new providers are offering compliance services at much lower costs than anticipated); JumperCard Letter; Kemp Letter; Leverage PR Letter; Sfinarolakis Letter; StartEngine Letter 1 (noting that reviews and audits will be in the range of $1,500-$10,000 for smaller, newer companies); StartEngine Letter 2 (noting the emergence of third-party service providers); tempCFO Letter; Upchurch Letter (stating that the market will adjust for costs).

310 For supporters, *see, e.g.*, AICPA Letter (for offerings over $100,000); CFA Institute Letter; EY Letter (for offerings over $100,000 for only the most recent year); Hackers/Founders Letter; Heritage Letter (recommending for issuers with assets over $100,000, that if financial statements are not prepared in accordance with U.S. GAAP, the issuer be required to note any variance from U.S. GAAP and state the reason for such variance); NASAA Letter; RocketHub Letter; Whitaker Chalk Letter (for offerings over $500,000 until such time as the Commission accepts IFRS for U.S. domestic issuers).

For opponents, *see, e.g.*, ABA Letter (noting that the benefits associated with GAAP-compliant financial statements do not outweigh the burdens that mandatory application of GAAP would impose); CrowdCheck Letter 4; EarlyShares Letter; Graves Letter (recommending that U.S. GAAP only be required for issuers with $5 million in revenue); Milken Institute Letter (recommending that U.S. GAAP only be required for issuers with $5 million in revenue, the threshold at which the IRS requires a switch to accrual accounting); Public Startup Letter 2; SBEC Letter (noting the AICPA's release of new guidelines in June 2013 for small and mid-size businesses); Tiny Cat Letter; U.S. Chamber of Commerce Letter; Wilson Letter (recommending

having a single standard to facilitate comparison of different issuers,[311] and also that U.S. GAAP would be more likely to provide investors with a fair representation of an issuer's financial position and results of operations than financial statements using a comprehensive basis of accounting other than U.S. GAAP.[312]

A number of commenters recommended that, as a less expensive alternative to requiring U.S. GAAP, the Commission allow financial statements prepared in accordance with a comprehensive basis of accounting other than U.S. GAAP.[313] Other commenters recommended that if financial statements prepared in accordance with U.S. GAAP are required, they only be required in certain circumstances.[314]

A few commenters recommended that issuers relying on Section 4(a)(6) be permitted to take advantage of the extended transition period applicable to private companies for complying

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that the Commission consider the stage of the business in determining whether to require compliance with U.S. GAAP); Zhang Letter.

311 *See, e.g.*, NASAA Letter.

312 *See, e.g.*, EY Letter.

313 *See, e.g.*, ABA Letter (for offerings of $100,000 or less, but stating that the Commission could require providing U.S. GAAP financial statements if available); AICPA Letter; CFIRA Letter 5; CFIRA Letter 7; CrowdCheck Letter 4; EarlyShares Letter; EY Letter (for offerings of $100,000 or less, unless U.S. GAAP financial statements are available); Grassi Letter; Graves Letter (for issuers with less than $5 million in revenue); Mahurin Letter (stating that simple Excel spreadsheets accompanied by bank records should meet the financial statement requirements); Milken Institute Letter (for early-stage issuers); NFIB Letter; SBEC Letter; StartupValley Letter; Tiny Cat Letter (for offerings of less than $500,000); Whitaker Chalk Letter (for offerings of less than $500,000 if the issuer has an asset or income level below a certain level).

314 *See, e.g.*, ABA Letter (suggesting that: (i) in offerings of $100,000 or less, the certifying principal executive officer could be required to represent that the issuer is unable to prepare financial statements in accordance with U.S. GAAP without unreasonable effort or expense; (ii) in offerings of more than $100,000, but not more than $500,000, the exception could also require the principal executive officer representation and be limited to issuers that have not prepared U.S. GAAP-compliant financial statements for any other purpose and who have no operating history, no revenues and/or a minimal amount of assets (*e.g.*, $500,000); and (iii) in offerings of more than $500,000, the exception could require the principal executive officer representation, including a representation that the other comprehensive basis of accounting methodology selected is acceptable under AICPA standards, and be limited to issuers with no operating history or revenue and minimal assets).

with new or revised accounting standards.[315] A few commenters expressed concern that Section 4(a)(6) issuers may be viewed as "public business entities" by FASB.[316] One commenter recommended that the Commission provide an exemption from this definition for such issuers.[317]

Periods Covered in the Financial Statements. While two commenters generally supported requiring two years of financial statements,[318] a number of commenters generally opposed the proposal, recommending one year of financial statements instead.[319] Many commenters opposed requiring interim financial statements,[320] while several supported such a requirement.[321] Several commenters recommended that if interim financial statements are required, they not be subject to audit or review,[322] while another commenter recommended that they not be filed with the Commission, but only be provided to investors.[323]

Age of Financial Statements. Several commenters opposed our proposal that financial statements be dated within 120 days of the start of the offering,[324] while one commenter supported

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315 *See, e.g.*, EY Letter; U.S. Chamber of Commerce Letter.

316 *See, e.g.*, ABA Letter; EY Letter (noting also the definition of "public entity" under the Accounting Standards Codification).

317 *See* EY Letter.

318 *See* ASSOB Letter; Zeman Letter.

319 *See, e.g.*, Denlinger Letter 1; EY Letter; Grassi Letter; Joinvestor Letter; Public Startup Letter 2; RFPIA Letter (as it relates to audited financial statements); RocketHub Letter; Verrill Dana Letter.

320 *See, e.g.*, CFIRA Letter 7; EMKF Letter; EY Letter; FundHub Letter 1; Grassi Letter; Public Startup Letter 2; RocketHub Letter; Traklight Letter; Wefunder Letter; Whitaker Chalk Letter.

321 *See, e.g.*, AICPA Letter; Consumer Federation Letter (recommending supplementing the proposed financial statement requirements with unaudited CEO-certified financial statements through the end of the month ending no more than two months before the offering begins); Denlinger Letter 1 (recommending quarterly basic financial reporting, including a balance sheet, income statement and statement of cash flows); Fund Democracy Letter.

322 *See, e.g.*, CFIRA Letter 7; Consumer Federation Letter; Denlinger Letter 1; Fund Democracy Letter; Traklight Letter.

323 *See* RocketHub Letter.

324 *See, e.g.*, Grassi Letter; Public Startup Letter 2; RocketHub Letter.

it.[325] Some commenters opposed our proposal to permit an issuer, during the first 120 days of the issuer's fiscal year, to conduct an offering in reliance on Section 4(a)(6) using financial statements for the fiscal year prior to the most recently completed fiscal year,[326] while two others supported such accommodation.[327] One commenter recommended that, to provide "truly current financials" for large offerings, the Commission could require unaudited financial statements through the end of the month that ends no more than two months before the month in which the offering begins (*e.g.*, an offering any day in March would require financials up to January 31); for smaller offerings, the commenter indicated a modified standard for providing current information might be appropriate.[328]

Public Accountant Requirements. We received several comments on standards for audit firms.[329] Commenters supported not requiring audits to be conducted by a PCAOB-registered firm.[330] Some commenters supported our proposal to require the public accountant reviewing or

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325 *See* Denlinger Letter 1.

326 *See, e.g.*, Consumer Federation Letter (stating that the proposal allows for the provision of stale and limited financial information because it "would allow issuers to submit financial statements that are more than a year out of date and that cover only a very limited portion of the issuer's existence."); EY Letter (recommending this time period be extended to 180 days if an issuer presents interim financial statements certified by the principal executive officer that cover the first six months of the issuer's most recently completed fiscal year); Fund Democracy Letter (noting that financial statements could be 16-months stale); Merkley Letter (recommending that the Commission not permit financial statements "to be so thoroughly out of date"); Public Startup Letter 2.

327 *See, e.g.*, Grassi Letter (noting that the material change disclosure requirements should be sufficient to keep investors updated); RocketHub Letter.

328 *See* Fund Democracy Letter.

329 *See, e.g.*, Grassi Letter (recommending no audit be accepted that has been performed by a firm that is not subject to, or that has received a fail report under, the AICPA peer review standards); ASSOB Letter (recommending the rules not place restrictions on the type of accountant an issuer is required to use to review or audit its financial statements); Multistate Tax Letter (an issuer should not be required to obtain accounting services).

330 *See, e.g.*, AICPA Letter; ASSOB Letter (recommending the rules not place restrictions on the type of accountant an issuer is required to use to review or audit its financial statements); Denlinger Letter 1; Funderbuddies Letter; EY Letter; Grassi Letter; Heritage Letter; Multistate Tax Letter (an issuer should not be required to obtain accounting services); Public Startup Letter 2; RocketHub Letter; Traklight Letter. *See*

auditing an issuer's financial statements to comply with the independence requirements set forth in Rule 2-01 of Regulation S-X,[331] while other commenters recommended allowing the public accountant to comply by meeting the independence requirements of the AICPA.[332] Some commenters noted that many startups and early-stage small businesses require assistance in the preparation of financial statements, and that complying with the independence standards of Regulation S-X would require such issuers to engage two external accountants – one to assist in preparing the financial statements and another to audit or review them.[333] One commenter asked the Commission not to create new independence standards.[334]

Review and Audit Standards. With respect to review standards, commenters supported requiring reviewed financial statements to be reviewed in accordance with the SSARS issued by the AICPA.[335] Commenters also opposed creating a new set of review standards.[336]

With respect to audit standards, several commenters supported our proposal to require that financial statements be audited in accordance with the auditing standards issued by either the AICPA or the PCAOB,[337] while several others opposed it.[338] Two commenters recommended that

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also RFPIA Letter (recommending the public accountants conducting an audit be required to be members of the AICPA or the PCAOB for one year.).

331 *See, e.g.*, ABA Letter; Commonwealth of Massachusetts Letter; RocketHub Letter.

332 *See, e.g.*, AICPA Letter; Denlinger Letter 1; EY Letter; Grassi Letter; McGladrey Letter.

333 *See, e.g.*, AICPA Letter; EY Letter; Grassi Letter.

334 *See* AICPA Letter (recommending that the Commission not create new independence, review, or auditing standards or that the definition of "a complete set of financial statements" be different than under U.S. GAAP because doing so would result in confusion, further complexity and increased costs).

335 *See, e.g.*, ABA Letter; AICPA Letter; Denlinger Letter 1; EY Letter; Fund Democracy Letter; Grassi Letter. *But see* Public Startup Letter 2.

336 *See, e.g.*, AICPA Letter; Denlinger Letter 1; Grassi Letter; Traklight Letter.

337 *See, e.g.* AICPA Letter; Denlinger Letter 1; EY Letter; Grassi Letter.

338 *See, e.g.*, Consumer Federation Letter; Fund Democracy Letter; Public Startup Letter 2; RocketHub Letter; Rucker Letter (stating that GAAS fit poorly with the kinds of businesses Title III is intended to accommodate).

audits be required to be conducted in accordance with the auditing standards issued by the PCAOB.[339] Commenters generally opposed creating a new set of audit standards,[340] although one commenter recommended that if the Commission were to create a new set of audit standards, it "should be designed as an ultra-low-cost procedure."[341]

Review and Audit Reports. With respect to review reports, two commenters supported our proposal that a review report that includes modifications would satisfy the reviewed financial statement requirement,[342] while one commenter opposed it.[343] With respect to audit reports, commenters supported our proposal that a qualified audit opinion would satisfy the audited financial statement requirements,[344] although one commenter opposed it.[345] One commenter requested clarification as to the requirements that may be applicable to the issuer and the public accountant when an issuer intends to include a previously issued audit or review report in an offering statement.[346]

Exemptions from Financial Statement Requirements. While the proposed rules did not exempt any issuers from the financial statement requirements, a number of commenters

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339 *See* Consumer Federation Letter; Fund Democracy Letter.

340 *See, e.g.*, AICPA Letter; Grassi Letter (recommending that the Commission require issuers to use the same standards used in the offering or higher standards, with the PCAOB standards deemed to be the higher standard, when complying with the ongoing reporting requirements); Heritage Letter; Traklight Letter.

341 RocketHub Letter.

342 *See* AICPA Letter; Heritage Letter (for going concern opinions).

343 *See* Grassi Letter.

344 *See, e.g.*, AICPA Letter; Arctic Island Letter 5 (noting that most small business audit opinions are likely to include a going concern clause); Denlinger Letter 1 (noting, however, that a going concern opinion is not a qualified opinion); EY Letter; Heritage Letter (noting that a majority of crowdfunding issuers should receive going concern opinions but should not be disqualified); RocketHub Letter; Traklight Letter (recommending that going concern opinions and noncompliance with U.S. GAAP should be allowed); Whitaker Chalk Letter.

345 *See* Grassi Letter.

346 *See* EY Letter.

recommended exempting issuers with no operating history or issuers that have been in existence for fewer than 12 months from the requirement to provide financial statements,[347] although a few commenters opposed such a concept.[348] A number of commenters recommended that if an exemption for such issuers is allowed, the exempted issuers should provide certain basic disclosures,[349] and two commenters specifically recommended that if an exemption for such issuers is allowed, the exempted issuers should still provide a balance sheet.[350]

(iii) Final Rules

We are adopting financial disclosure requirements for Title III issuers in Rule 201(t) with a number of changes from the proposal. As described in more detail below, the final requirements are based on the amount offered and sold in reliance on Section 4(a)(6) within the preceding 12-month period, as follows:

- For issuers offering $100,000 or less: disclosure of the amount of total income, taxable income and total tax as reflected in the issuer's federal income tax returns certified by the principal executive officer to reflect accurately the information in the issuer's federal income tax returns (in lieu of filing a copy of the tax returns), and financial statements certified by the principal executive officer to be true and complete in all material

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347 *See, e.g.*, Arctic Island Letter 5 (supporting only an exemption from the audit requirement); CFIRA Letter 5; CFIRA Letter 7; CrowdFundConnect Letter; Crowdpassage Letter 2; EY Letter; Grassi Letter; Hackers/Founders Letter; Joinvestor Letter; McGladrey Letter; PBA Letter; PeoplePowerFund Letter; RocketHub Letter (recommending that the audit requirements should only apply to issuers that have been in operation for more than two years and are raising more than $5 million); StartupValley Letter (supporting an exemption from the audit requirements); Wefunder Letter; Whitaker Chalk Letter.

348 *See, e.g.*, AICPA Letter; Denlinger Letter 1; Wilson Letter.

349 *See, e.g.*, ASSOB Letter; CFIRA Letter 5; Denlinger Letter 1; Grassi Letter; McGladrey Letter; PBA Letter; PeoplePowerFund Letter; RocketHub Letter; Wefunder Letter; Whitaker Chalk Letter; Zhang Letter.

350 *See* EY Letter; PBA Letter.

respects.[351] If, however, financial statements of the issuer are available that have either been reviewed or audited by a public accountant that is independent of the issuer, the issuer must provide those financial statements instead and need not include the information reported on the federal income tax returns or the certification of the principal executive officer.

- Issuers offering more than $100,000 but not more than $500,000: financial statements reviewed by a public accountant that is independent of the issuer.[352] If, however, financial statements of the issuer are available that have been audited by a public accountant that is independent of the issuer, the issuer must provide those financial statements instead and need not include the reviewed financial statements.
- Issuers offering more than $500,000:
    - For issuers offering more than $500,000 but not more than $1 million of securities in reliance on Regulation Crowdfunding for the first time: financial statements reviewed by a public accountant that is independent of the issuer. If, however, financial statements of the issuer are available that have been audited by a public accountant that is independent of the issuer, the issuer must provide those financial statements instead and need not include the reviewed financial statements.
    - For issuers that have previously sold securities in reliance on Regulation Crowdfunding: financial statements audited by a public accountant that is independent of the issuer.[353]

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351 *See* Rule 201(t)(1) of Regulation Crowdfunding.

352 *See* Rule 201(t)(2) of Regulation Crowdfunding.

353 *See* Rule 201(t)(3) of Regulation Crowdfunding. *See also* discussion below under "Offerings of more than $500,000."

Content of Financial Statements. We are adopting substantially as proposed the requirement that all issuers file with the Commission and provide to investors and the relevant intermediary a complete set of their financial statements, which includes balance sheets, statements of comprehensive income, statements of cash flows, statements of changes in stockholders' equity and notes to the financial statements.[354] In order to avoid potential confusion as to the presentation of financial statements, and consistent with Tier 1 offerings under Regulation A,[355] the final rule adds an instruction that financial statements that are not audited must be labeled as unaudited.[356] Consistent with the proposal, the final rules do not exempt any issuers from the financial statement requirements. Although some commenters expressed concerns about the costs of the financial statement requirements for issuers with no operating history or issuers that have been in existence for fewer than 12 months,[357] we believe that financial statements are important information for investors and that the changes from the proposed rules described below will help reduce the costs associated with preparing financial statements for many of those issuers.

The final rule also includes an instruction to clarify that references to the issuer in Rule 201(t) refer to the issuer and its predecessors, if any.

Offerings of $100,000 or less. Consistent with Securities Act Section 4A(b)(1)(D)(i), we are adopting as proposed the requirement in Rule 201(t)(1) that an issuer offering $100,000 or less

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354 *See* Instruction 3 to paragraph (t) of Rule 201 of Regulation Crowdfunding.

355 *See* Paragraph (b) of Part F/S of Form 1-A.

356 *See* Instruction 3 to paragraph (t) of Rule 201 of Regulation Crowdfunding.

357 *See, e.g.*, Arctic Island Letter 5; CFIRA Letter 5; CFIRA Letter 7; CrowdFundConnect Letter; Crowdpassage Letter 2; EY Letter; Grassi Letter; Hackers/Founders Letter; Joinvestor Letter; McGladrey Letter; PBA Letter; PeoplePowerFund Letter; RocketHub Letter; StartupValley Letter; Wefunder Letter; Whitaker Chalk Letter. *But see* AICPA Letter; Denlinger Letter 1; Wilson Letter.

provide financial statements of the issuer that are certified by the principal executive officer of the issuer to be true and complete in all material respects.[358] While we believe it will be beneficial for investors to have an independent accountant review financial statements in offerings over $100,000, we believe that for offerings of $100,000 or less this certification is sufficient and will contribute to the integrity of the issuer's financial reporting process. It will affirm for investors that, although the financial statements have not been reviewed or audited by an independent public accountant, there has been senior executive attention paid to the financial statements. We are not requiring this certification for reviewed or audited financial statements, as some commenters suggested, because we believe the certification is intended as an added measure of assurance that is not needed in offerings of this size when an independent accountant reviews or audits the financial statements. We also are adopting the form of the certification that must be provided by the issuer's principal executive officer as proposed with one change relating to the information from the issuer's tax return.[359]

Instead of mandating that issuers offering $100,000 or less provide copies of their federal income tax returns as proposed, the final rules require an issuer to disclose the amount of total income, taxable income and total tax, or the equivalent line items from the applicable form, exactly as reflected in its filed federal income tax returns, and to have the principal executive officer certify that those amounts reflect accurately the information in the issuer's federal income tax returns.[360] As noted by commenters,[361] requiring that issuers provide tax returns may present

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358 *See* Rule 201(t)(1) of Regulation Crowdfunding.

359 *See* Instruction 7 to paragraph (t) of Rule 201 of Regulation Crowdfunding.

360 *See* Rule 201(t)(1) of Regulation Crowdfunding.

361 *See, e.g.*, AICPA Letter; Public Startup Letter 2; RocketHub Letter; SBM Letter; Wilson Letter; Zhang Letter.

a significant risk of disclosure of private information. While the proposed rule would require personally identifiable information to be redacted, we are persuaded by commenters that such a requirement might not provide an adequate safeguard against inadvertent disclosure of this type of information in some instances. The consequences for an issuer and an intermediary of such disclosure, including the potential violation of applicable privacy laws, could be severe. Specifying the information from the tax return that is required without requiring submission of the tax return itself will provide standardized disclosure for investors and help protect against the accidental disclosure of personally identifiable or confidential information. Requiring that these amounts be certified by the principal executive officer will provide investors additional assurance of the accuracy of those amounts in lieu of providing the underlying tax returns.[362] At the same time, because the principal executive officer will be certifying only that the amounts are as reported on the applicable income tax return, we do not expect this requirement to impose any significant new burdens on principal executive officers, who will already be certifying as to the truth and completeness of the financial statements themselves. We believe the alternative approach we are adopting provides a similar benefit to investors as the proposal while addressing the privacy concerns raised by commenters.

As we stated in the Proposing Release, it remains unclear to us to what extent all of the information presented in a tax return would be useful for an investor evaluating whether to purchase securities from the issuer. We believe, however, that certain information such as total income, taxable income and total tax could be informative and would likely be available to the issuer in tax documentation. The final rules, therefore, provide that an issuer must disclose its

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[362] We note that any intentional misstatements or omissions of facts may constitute federal criminal violations by the certifying principal executive officer. *See* 18 U.S.C. 1001.

total income, taxable income and total tax, or the equivalent line items from its federal income tax documentation and have the principal executive officer certify that those amounts reflect accurately the information in the issuer's federal income tax returns.[363]

Under the final rules, an issuer that offers securities in reliance on Section 4(a)(6) before filing its tax return for the most recently completed fiscal year will be allowed to use information from the tax return filed for the prior year. An issuer that uses information from the prior year's tax return will be required to provide tax return information for the most recently completed fiscal year when filed with the U.S. Internal Revenue Service (if the tax return is filed during the offering period). An issuer that has requested an extension from the U.S. Internal Revenue Service would not be required to provide the information until the date when the return is filed, which is consistent with the concept of not requiring tax information until that information has been filed with the U.S. Internal Revenue Service. If an issuer has not yet filed a tax return and is not required to file a tax return before the end of the offering period, then the tax return information does not need to be provided.[364]

We are adding to Rule 201(t)(1) a requirement that if financial statements of the issuer are available that have either been reviewed or audited by a public accountant that is independent of the issuer, the issuer must provide those financial statements instead, and need not include the information reported on the federal income tax returns or the certification of the principal executive officer.[365] This approach was suggested by two commenters,[366] and we believe it will benefit investors by providing access to audited or reviewed financial statements that were already

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363 *See* Rule 201(t)(1) of Regulation Crowdfunding.

364 *See* Instruction 6 to paragraph (t) of Rule 201 of Regulation Crowdfunding.

365 *See* Rule 201(t)(1) of Regulation Crowdfunding.

366 *See* Angel Letter 1; EY letter.

prepared for other purposes. Unlike audit reports in a registered offering,[367] we are not requiring that review or audit reports be accompanied by a formal consent or acknowledgment letter. Rather, the final rules clarify that review and audit reports must be signed and that the issuers must notify the public accountants of their intended use in an offering in reliance on Section 4(a)(6).[368]

Offerings of more than $100,000 but not more than $500,000. Consistent with Section 4A(b)(1)(D)(iii) and the proposed rules, issuers must file and provide reviewed financial statements when offering more than $100,000 but not more than $500,000.[369] Similar to the addition to Rule 201(t)(1) discussed above, we have added to Rule 201(t)(2) a requirement that if financial statements of the issuer are available that have been audited by a public accountant that is independent of the issuer, the issuer must provide those financial statements instead.[370] The approach of providing audited financial statements that are otherwise available is consistent with what the Commission adopted for issuers undertaking Tier 1 offerings under Regulation A.[371] We believe the benefits to investors of having access to these audited financial statements justify any additional burden imposed on issuers to provide these statements, which were already prepared for other purposes.

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367 *See* Securities Act Rule 436; Item 601 of Regulation S-K.

368 *See* Instructions 8 and 9 to paragraph (t) of Rule 201 of Regulation Crowdfunding.

369 *See* Rule 201(t)(2) of Regulation Crowdfunding.

370 *Id*.

371 *See* Paragraph (b) of Part F/S of Form 1-A. While Regulation Crowdfunding incorporates a number of requirements that are consistent with Regulation A, it is important to note that Regulation Crowdfunding and Regulation A are different exemptions with distinct requirements. For example, unlike offerings under Regulation Crowdfunding, Tier 1 offerings under Regulation A are subject to state registration requirements and are required to be "qualified" by Commission staff.

Offerings of more than $500,000. As proposed, Rule 201(t)(3) provides that issuers offering more than $500,000 are required to provide audited financial statements. In a change from the proposal, the final rule includes an accommodation for issuers offering more than $500,000 but not more than $1 million that have not previously sold securities in reliance on Section 4(a)(6).[372] Under Rule 201(t)(3), those first-time issuers are permitted to provide reviewed rather than audited financial statements, unless audited financial statements are otherwise available.

We are adding this accommodation for first-time issuers in response to commenters' concerns about the expense of obtaining audited financial statements. While some commenters expressed support for the proposed audit requirement,[373] many others noted that the proposed audit requirement would be too costly and burdensome for issuers in comparison to the size of the offering proceeds.[374] A number of commenters expressed particular concern that issuers would need to incur the expense of an audit before having proceeds or even an assurance of proceeds from the offering.[375] After considering the comments, we are persuaded that for issuers undertaking a first-time crowdfunding offering of more than $500,000 but not more than $1

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372 For purposes of determining whether an issuer has previously sold securities in reliance on Section 4(a)(6), "issuer" includes all entities controlled by or under common control with the issuer and any predecessors of the issuer. *See* Rule 100(c) of Regulation Crowdfunding.

373 *See, e.g.*, AICPA Letter; Consumer Federation Letter; CSTTC Letter; Denlinger Letter 2; FundDemocracy Letter; Leverage PR; NASAA Letter; StartEngine Letter 1.

374 *See, e.g.*, AEO Letter; Angel Letter 1; AWBC Letter; CFIRA Letter 5; CfPA Letter; CrowdFundConnect Letter; EarlyShares Letter; EMKF Letter; EY Letter; Finkelstein Letter; FundHub Letter 1; Generation Enterprise Letter; Grassi Letter; Graves Letter; Guzik Letter 1; Hakanson Letter; Holland Letter; Johnston Letter; Kickstarter Coaching Letter; McGladrey Letter; Milken Institute Letter; NACVA Letter; NFIB Letter; NPCM Letter; NSBA Letter; PBA Letter; Reed Letter; RocketHub Letter; Saunders Letter; SBA Office of Advocacy Letter; SBEC Letter; SBM Letter; Seyfarth Letter; Verrill Dana Letter; WealthForge Letter; Wefunder Letter; Woods Letter; Zeman Letter.

375 *See, e.g.*, AEO Letter; AWBC Letter; CFIRA Letter 5; CfPA Letter; EMKF Letter; Generation Enterprise Letter; Grassi Letter; Graves Letter; Holland Letter; McGladrey Letter; NSBA Letter; Reed Letter; RocketHub Letter; SBM Letter; Seyfarth Letter; WealthForge Letter; Wefunder Letter.

million, the benefits of requiring audited financial statements are not likely to justify the costs. Accordingly, consistent with applicable standards,[376] for these first-time issuers, we are adopting instead a requirement that those selling securities in reliance on Section 4(a)(6) in these circumstances provide reviewed financial statements. Commenters stated that reviewed financial statements would cost less than audited financial statements,[377] and one commenter noted that the cost of an accounting review is approximately 60% of the cost of an audit.[378]

Basis of Accounting. We are adopting as proposed the requirement that all issuers provide financial statements prepared in accordance with U.S. GAAP.[379] As discussed in the Proposing Release, financial statements prepared in accordance with U.S. GAAP are generally self-scaling to the size and complexity of the issuer, which we believe can reduce the costs of preparing financial statements for many early stage issuers. We would not expect that the required financial statements would be long or complicated for issuers that are recently formed and have limited operating histories. Although we acknowledge, as some commenters observed, that other bases of accounting may be less expensive than U.S. GAAP, we believe the benefit of a single standard that will facilitate comparison among issuers relying on Section 4(a)(6) justifies any incremental expenses associated with U.S. GAAP. In addition, we are concerned that it may be difficult for investors to determine whether the issuer complied with another comprehensive basis of accounting. For these reasons, we continue to believe that financial statements prepared in

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376 *See* Securities Act Section 28 [15 U.S.C. 77z-3].

377 *See, e.g.*, Crowdcheck Letter 4; CfPA Letter (noting that many offerings made in reliance on Rule 506 that involve companies further along in their business development include reviewed but not audited financial statements); Graves Letter (discussing the "thorough" nature of a CPA review and the cost differential between reviewed and audited financial statements); NFIB Letter; Traklight Letter.

378 *See* Traklight Letter.

379 *See* Instruction 3 to paragraph (t) of Rule 201 of Regulation Crowdfunding.

accordance with U.S. GAAP will be the most useful for investors in securities-based crowdfunding transactions, particularly when presented along with the required description of the issuer's financial condition.[380]

Additionally, as suggested by one commenter,[381] in order to be consistent with the treatment of emerging growth companies[382] and offerings relying on Regulation A,[383] Rule 201(t) permits issuers, where applicable, to delay the implementation of new accounting standards to the extent such standards provide for delayed implementation by non-public business entities.[384] In this regard, if the issuer chooses to take advantage of this extended transition period, the issuer:

- Must disclose such choice at the time the issuer files the offering statement; and
- May not take advantage of the extended transition period for some standards and not others, but must apply the same choice to all standards.

However, consistent with the treatment of emerging growth companies and offerings relying on Regulation A,[385] issuers electing not to use this accommodation must forgo this accommodation for all financial accounting standards and may not elect to rely on this accommodation in any future filings.[386]

On December 23, 2013, after we proposed rules for Regulation Crowdfunding, the Financial Accounting Standards Board (FASB) and Private Company Council (PCC) issued a

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380 *See* Rule 201(s) of Regulation Crowdfunding.

381 S*ee* EY Letter.

382 *See* Securities Act of 1933 Section 7(a)(2)(B) [15 USC 77g(a)(2)(B)].

383 *See* paragraph (a)(3) of Part F/S of Form 1-A.

384 *See* Instruction 5 to paragraph (t) of Rule 201 of Regulation Crowdfunding.

385 *See* paragraph (a)(3) of Part F/S of Form 1-A. *See* also JOBS Act, Section 107(b)(1) and (3).

386 *See* Instruction 5 to paragraph (t) of Rule 201 of Regulation Crowdfunding.

guide for evaluating financial accounting and reporting for non-public business entities.[387] The PCC was created in 2012 by the FASB and the Financial Accounting Foundation to improve the standard-setting process, and provide for accounting and reporting alternatives, for non-public business entities under U.S. GAAP.[388] As the standards for non-public business entities are new, there are currently very few distinctions between U.S. GAAP for public and non-public business entities. Over time, however, more distinctions between non-public business entity and public company accounting standards could develop.

Issuers that offer securities pursuant to Regulation Crowdfunding will be considered "public business entities" as defined by the FASB[389] and, therefore, ineligible to rely on any alternative accounting or reporting standards for non-public business entities.[390] Even though issuers of securities in a Regulation Crowdfunding offering fit within the definition of "public business entity," the Commission retains the authority to determine whether or not such issuers would be permitted to rely on the developing non-public business entity standards.[391]

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387 The Private Company Decision-Making Framework: A Guide for Evaluating Financial Accounting and Reporting for Private Companies (the "PCC Guide"), *available at*: http://www.fasb.org/cs/ContentServer?c=Document_C&pagename=FASB%2FDocument_C%2FDocumentPage&cid=1176163703583.

388 For a brief history behind the creation of the PCC, *see*: http://www.fasb.org/cs/ContentServer?c=Page&pagename=FASB%2FPage%2FSectionPage&cid=1351027243391.

389 Criterion (a) of FASB's Accounting Standards Update 2013-12, *Definition of a Public Business Entity*, states that an entity that "is required by the U.S. Securities and Exchange Commission (SEC) to file or furnish financial statements, or does file or furnish financial statements (including voluntary filers), with the SEC (including other entities whose financial statements or financial information are required to be or are included in a filing)" is a Public Business Entity.

390 *See* numbered paragraph 12 of the PCC Guide, p. 3.

391 *Id*.

Commenters generally expressed concern about the costs associated with requiring issuers relying on Section 4(a)(6) to follow public company U.S. GAAP accounting standards.[392]

The final rules do not allow Regulation Crowdfunding issuers to use the alternatives available to non-public business entities under U.S. GAAP in the preparation of their financial statements. One of the significant factors considered by the FASB in developing its definition of "public business entity" was the number of primary users of the financial statements and their access to management.[393] As the FASB noted, "users of private company financial statements have continuous access to management and the ability to obtain financial information throughout the year."[394] As the number of investors increases and their ability individually to influence management decreases, it is important that all investors receive or have timely access to comprehensive financial information. As a result, although commenters generally expressed concern about the costs associated with requiring issuers relying on Section 4(a)(6) to follow public company U.S. GAAP accounting standards,[395] because crowdfunding investors will likely not have the access to management that the FASB envisions, the Commission believes that investor protection will be enhanced by requiring Regulation Crowdfunding issuers to provide financial statements prepared in the same manner as other entities meeting the FASB's definition of "public business entity."

Periods Covered in the Financial Statements. We are adopting substantially as proposed the requirement that financial statements cover the shorter of the two most recently completed

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392 *See, e.g.*, ABA Letter; CFIRA Letter 5; Grassi; EY Letter; U.S. Chamber of Commerce Letter.

393 *See* PCC Guide, p. 6.

394 *Id.*

395 *See, e.g.*, ABA Letter; CFIRA Letter 5; Grassi; EY Letter; U.S. Chamber of Commerce Letter.

fiscal years or the period since the issuer's inception.[396] While a number of commenters recommended only one year of financial statements,[397] we believe that requiring a second year will provide investors with a basis for comparison against the most recently completed period, without substantially increasing the costs for the issuer.

In addition, consistent with the proposal and with the views of many commenters,[398] the final rules do not require interim financial statements. While we recognize the needs of investors for current financial information, we are also cognizant of the anticipated costs of obtaining interim financial statements. We believe that the required discussion of any material changes or trends known to management in the financial condition and results of operations of the issuer since the period for which financial statements are provided will help provide investors with the necessary information.[399]

Age of Financial Statements. We are adopting substantially as proposed rules providing that during the first 120 days of the issuer's fiscal year, an issuer may conduct an offering in reliance on Section 4(a)(6) using financial statements for the fiscal year prior to the most recently completed fiscal year if the financial statements for the most recently completed fiscal year are not otherwise available.[400] For example, if an issuer that has a calendar fiscal year end conducts an offering in April 2016, it would be permitted to include financial statements for the fiscal year

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396 *See* Instruction 3 to paragraph (t) of Rule 201 of Regulation Crowdfunding.

397 *See, e.g.*, Denlinger Letter 1; EY Letter; Fryer Letter; Grassi Letter; Joinvestor Letter; Public Startup Letter 2; RFPIA Letter; RocketHub Letter. *But see, e.g.*, ASSOB Letter; Zeman Letter.

398 *See, e.g.*, CFIRA Letter 7; EMKF Letter; EY Letter; FundHub Letter 1; Grassi Letter; Public Startup Letter 2; RocketHub Letter; Traklight Letter; Wefunder Letter; Whitaker Chalk Letter.

399 *See* Instruction 1 to paragraph (s) of Rule 201 of Regulation Crowdfunding.

400 *See* Instruction 4 to paragraph (t) of Rule 201 of Regulation Crowdfunding. The final rule incorporates instructions consistent with other SEC rules explaining that if the 120th day falls on a Saturday, Sunday, or holiday, the next business day shall be considered the 120th day.

ended December 31, 2014 if the financial statements for the fiscal year ended December 31, 2015 are not yet available. Once more than 120 days have passed since the end of the issuer's most recently completed fiscal year, the issuer would be required to include financial statements for its most recently completed fiscal year.[401] Regardless of the age of the financial statements, an issuer would be required to include in the narrative discussion of its financial condition a discussion of any material changes or trends known to management in the financial condition and results of operations of the issuer during any time period subsequent to the period for which financial statements are provided to inform investors of more recent developments.[402]

While some commenters expressed concern that this accommodation would not provide investors with sufficiently current financial information,[403] we believe that this risk will be mitigated by the requirement that the issuer include a narrative discussion of any material changes or trends known to management in the financial condition and results of operations during any time period subsequent to the period for which financial statements are provided.[404] Further, we believe this accommodation is needed because otherwise issuers would not be able to conduct offerings for a period of time between the end of their fiscal year and the date when the financial statements for that period are available.

We are not adopting the alternative proposed by one commenter to require unaudited financial statements through the end of the month that ends no more than two months before the month in which the offering began.[405] Such a requirement would require an issuer to prepare a set

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401 *Id.*

402 *See* Rule 201(s) of Regulation Crowdfunding and Instruction 1 to paragraph (s) of Rule 201.

403 *See, e.g.*, Consumer Federation Letter; Fund Democracy Letter; Merkley Letter.

404 *See* Rule 201(s) of Regulation Crowdfunding and instruction 1 to paragraph (s) of Rule 201.

405 *See* Fund Democracy Letter.

of financial statements at a time when it would not otherwise be doing so and would be a more onerous requirement than applies to registered or Regulation A offerings.[406]

Public Accountant Requirements. In a change from proposed Rule 201(t), in response to commenters' suggestions, the final rules provide that to qualify as independent of the issuer, a public accountant would be required to either: (1) comply with the Commission's independence rules, which are set forth in Rule 2-01 of Regulation S-X,[407] or (2) comply with the independence standards of the AICPA.[408] Allowing the AICPA independence standards as an alternative to the Commission's independence standards is consistent with the recommendations of a number of commenters[409] and the treatment of Tier 1 issuers under Regulation A.[410] We believe that providing issuers with this flexibility is appropriate in light of the potential costs to issuers that would otherwise be required to engage an accountant who was independent under Rule 2-01 of Regulation S-X.

Consistent with the recommendation of one commenter,[411] in addition to meeting the independence standards of Rule 2-01 of Regulation S-X or the AICPA, we are requiring that a public accountant that audits or reviews the financial statements provided by an issuer must meet the standards for public accountants of Rule 2-01(a) of Regulation S-X. The Commission will not

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406 *See* Rule 3-12(a) of Regulation S-X [17 CFR 210.3-12(a)] (requires that the latest balance sheet be as of a date no more than 134 days for non-accelerated filers (or 129 days for accelerated and large accelerated filers) before the effective date of a registration statement (or date a proxy statement is mailed)); Paragraph (b) of Part F/S of Form 1-A (Tier 1 and Tier 2 issuers are required to include financial statements in Form 1-A that are dated not more than nine months before the date of non-public submission, filing, or qualification, with the most recent annual or interim balance sheet not older than nine months).

407 17 CFR 210.2-01.

408 *See* Instruction 9 to paragraph (t) of Rule 201 of Regulation Crowdfunding.

409 *See, e.g.*, AICPA Letter; Denlinger Letter 1; EY Letter; Grassi Letter; McGladrey Letter.

410 *See* Paragraph (b)(2) of Part F/S of Form 1-A. *See also, supra*, note 371.

411 *See* AICPA Letter.

recognize as a public accountant any person who: (1) is not duly registered and in good standing as a certified public accountant under the laws of the place of his residence or principal office; or (2) is not in good standing and entitled to practice as a public accountant under the laws of the place of his residence or principal office.[412] We believe these standards will promote the use of qualified accountants that are in compliance with the requirements for their profession for the review or audit of the financial statements with respect to all offerings, including offerings in reliance on Section 4(a)(6).

Consistent with the proposal and recommendations in response to our request for comments, we are not requiring audits to be conducted by a PCAOB-registered firm. We believe the final rules will result in a greater number of public accountants being eligible to audit the issuers' financial statements, which may reduce issuers' costs.

Review and Audit Standards. In line with the general support received from commenters,[413] we are adopting as proposed the requirement that reviewed financial statements be reviewed in accordance with the SSARS issued by the AICPA.[414] We also are adopting as proposed the requirement that audited financial statements, to the extent they are otherwise available, be audited in accordance with either the auditing standards of the AICPA (referred to as U.S. Generally Accepted Auditing Standards or GAAS) or the standards of the PCAOB.[415] We expect that this provision will provide issuers with more flexibility to file audited financial statements that may have been prepared for other purposes.

We believe that audits conducted in accordance with U.S. GAAS will provide sufficient

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412 *See* 17 CFR 210.2-01(a).

413 *See, e.g.*, ABA Letter; AICPA Letter; Denlinger Letter 1; EY Letter; Fund Democracy Letter; Grassi Letter.

414 *See* Instruction 8 to paragraph (t) of Rule 201 of Regulation Crowdfunding.

415 *See* Instruction 9 to paragraph (t) of Rule 201 of Regulation Crowdfunding.

protection for investors in these offerings, especially in light of the requirement that auditors must be independent under Rule 2-01 of Regulation S-X or AICPA independence standards. Moreover, we believe that the flexibility adopted in the final rules is appropriately tailored for the different types of issuers that are likely to conduct offerings under Regulation Crowdfunding.

Because issuers under Regulation Crowdfunding are not "issuers" as defined by Section 2(a)(7) of the Sarbanes-Oxley Act of 2002 nor broker-dealers registered with the Commission under Section 15(b) of the Securities Exchange Act of 1934, AICPA rules would require the audit to be compliant with U.S. GAAS even if the auditor has conducted the audit in accordance with PCAOB standards. Staff of the Commission consulted with the AICPA on this issue and has been advised that an audit performed by its members of an issuer conducting an offering under Regulation Crowdfunding would be required to comply with U.S. GAAS in accordance with the AICPA's Code of Professional Conduct.[416] As a result, an auditor for such an issuer who is conducting its audit in accordance with PCAOB standards also will be required to comply with U.S. GAAS, and the auditor will be required to comply with the reporting requirements of both the AICPA standards and the PCAOB standards. Commission staff also consulted with the AICPA on whether an auditor can currently comply with both sets of standards when issuing its auditor's report. In August 2015, the Auditing Standards Board of the AICPA proposed an amendment[417] to its auditing standards for situations when the auditor plans to refer to the standards of the PCAOB in addition to U.S. GAAS in the auditor's report. To comply with

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416 The AICPA Code of Professional Conduct is available at: http://pub.aicpa.org/codeofconduct/ethicsresources/et-cod.pdf.

417 Proposed Statement on Auditing Standards, *Amendment to Statement on Auditing Standards No. 122,* Statement on Auditing Standards: Clarification and Recodification, *section 700,* Forming an Opinion and Reporting on Financial Statements. The proposed amendment would be effective for audits of financial statements for periods ending on or after December 15, 2015.

the reporting requirements of both sets of standards in those situations, the proposed amendment would require the auditor to use the report layout and wording specified by the auditing standards of the PCAOB, amended to indicate that the audit was also conducted in accordance with U.S. GAAS.

Review and Audit Reports. We are adopting, with changes from the proposal, the requirement that issuers file with the Commission and provide to investors and the relevant intermediary a signed review or audit report on the issuer's financial statements by an independent public accountant.[418] The issuer must notify the public accountant of the issuer's intended use of the report in the offering.[419]

We are adopting as proposed the provision that an audit report that includes an adverse opinion or disclaimer of opinion will not be in compliance with the audited financial statement requirements.[420] In a change from the proposal, as suggested by one commenter,[421] the final rules do not permit a qualified audit report.[422] As noted above, under the final rules an issuer is not required to provide audited financial statements for first-time crowdfunding offerings of more than $500,000 but not more than $1 million unless otherwise available. We believe that this change reduces the cost and burden for issuers generally of providing audited financial statements, and that an accommodation to permit qualified audit reports is not necessary.

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418 *See* Instructions 8 and 9 to paragraph (t) of Rule 201 of Regulation Crowdfunding.

419 *Id*.

420 *See* Instruction 9 to paragraph (t) of Rule 201 of Regulation Crowdfunding.

421 *See* Grassi Letter.

422 *See* Instruction 9 to paragraph (t) of Rule 201 of Regulation Crowdfunding. Accordingly, a qualified audit opinion would not be considered an audit opinion that is "available" for purposes of Rule 201(t) and 202(a).

The final rules also provide that a review report that includes modifications will not satisfy the requirement for reviewed financial statements.[423] Although two commenters expressed that a review report with modifications should be sufficient to satisfy the reviewed financial statement requirement,[424] one commenter opposed permitting modifications to review reports, noting that it considers certain departures from U.S. GAAP to be "unacceptable" and that it would not be feasible to develop a model of all allowable and disallowable modifications.[425] After considering the comments, we are persuaded that permitting modifications could result in financial statements that depart materially from U.S. GAAP, and, therefore, are not permitting modifications to review reports under the final rules. In response to concerns expressed by some commenters, however, we note that a review report or audit opinion that includes explanatory language pertaining to the entity's ability to continue as a going concern is not, under current auditing standards, a modified report or a qualified opinion.[426]

Exemptions from Financial Statement Requirements. Consistent with the proposal, the final rules do not exempt any issuers from the financial statement requirements. While we appreciate the concerns identified by commenters about the costs of the financial statement requirements for issuers with no operating history or issuers that have been in existence for fewer than 12 months,[427] we believe that financial statements are important information for all issuers

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423 *See* Instruction 8 to paragraph (t) of Rule 201 of Regulation Crowdfunding. Accordingly, a modified review report would not be considered an audit opinion that is "available" for purposes of Rule 201(t) and 202(a).

424 *See* AICPA Letter; Heritage Letter.

425 *See* Grassi Letter.

426 *See, e.g.*, Public Company Accounting Oversight Board AU sec. 508, *Reports on Audited Financial Statements.*

427 *See, e.g.*, Arctic Island Letter 5; CFIRA Letter 5; CFIRA Letter 7; CrowdFundConnect Letter; Crowdpassage Letter 2; EY Letter; Grassi Letter; Hackers/Founders Letter; Joinvestor Letter; McGladrey Letter; PBA Letter; PeoplePowerFund Letter; RocketHub Letter; StartupValley Letter; Wefunder Letter; Whitaker Chalk Letter.

and that other changes from the proposed rules such as raising the threshold at which audited financial statements are required will help reduce those costs.

b. Progress Updates

(1) Proposed Rules

Consistent with Securities Act Section 4A(b)(1)(F), proposed Rule 201(v) and Rule 203(a)(3) of Regulation Crowdfunding would require an issuer to file with the Commission and provide investors and the relevant intermediary regular updates on the issuer's progress in meeting the target offering amount no later than five business days after each of the dates that the issuer reaches particular intervals – *i.e.*, 50 percent and 100 percent – of the target offering amount. If the issuer will accept proceeds in excess of the target offering amount, the issuer also would be required to file with the Commission and provide investors and the relevant intermediary a final progress update, no later than five business days after the offering deadline, disclosing the total amount of securities sold in the offering. If, however, multiple progress updates are triggered within the same five business-day period (*e.g.*, the issuer reaches 50 percent of the target offering amount on November 5, 100 percent of the target offering amount on November 7, and the maximum amount of proceeds it will accept in excess of the target offering amount on November 9), the issuer could consolidate such progress updates into one Form C-U, so long as the Form C-U discloses the most recent threshold that was met and the Form C-U is filed with the Commission and provided to investors and the relevant intermediary by the day on which the first progress update would be due. The proposed rules also would require the intermediary to make these updates available to investors through the intermediary's platform.

(2) Comments on the Proposed Rules

Commenters were generally opposed to the progress update requirements, noting that progress updates filed with the Commission would be duplicative of what is available from the intermediary's website and generate unnecessary costs.[428] Based on that same rationale, a number of commenters supported the concept of exempting issuers from the requirement to file progress updates with the Commission so long as the intermediary publicly displays the progress of the issuer in meeting the target offering amount.[429]

(3) Final Rules

The final rules maintain the proposed progress update requirements, with a significant modification. Based on concerns expressed by commenters, the final rules permit issuers to satisfy the progress update requirement by relying on the relevant intermediary to make publicly available on the intermediary's platform frequent updates about the issuer's progress toward meeting the target offering amount.[430] However, if the intermediary does not provide such an update, the issuer would be required to file the interim progress updates. In addition, as described in more detail below, an issuer relying on the intermediary's reports of progress must still file a Form C-U at the end of the offering to disclose the total amount of securities sold in the offering.[431]

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428 *See, e.g.*, ASSOB Letter; EarlyShares Letter; Public Startup Letter 2; RFPIA Letter; RocketHub Letter. *But see* CFIRA Letter 7.

429 *See, e.g.*, Arctic Island Letter 5 (stating that intermediaries can display both text (*e.g.* "$125,000 of $500,000 raised thus far") and graphics (*e.g.* a status bar graph) of the offering progress); ASSOB Letter; PeoplePowerFund Letter; RFPIA Letter; RocketHub Letter (noting that portals already list progress for perks-based crowdfunding); Wefunder Letter. *But see* CFIRA Letter 7 (stating that the issuer should file progress updates with the Commission on a regular basis to allow for consistency across all issuers and intermediaries.).

430 *See* Rules 201(v) and 203(a)(3) of Regulation Crowdfunding.

431 *See* Rule 203(a)(3)(iii) of Regulation Crowdfunding.

As stated in the proposal, we continue to believe that the information available in progress updates will be important to investors by allowing them to gauge whether interest in the offer has increased gradually or whether it was concentrated at the beginning or at the end of the offering period. We believe that these same benefits can be achieved through information available on the intermediary's platform about the progress toward the target offering amount. Whether an issuer provides the required progress update report or relies on the intermediary's reporting, we believe investors will benefit by being able to stay informed during the offering of an issuer's progress.

Under the final rules, all issuers must file a Form C-U to report the total amount of securities sold in the offering. For issuers that are offering only up to a certain target offering amount, this requirement will be triggered five business days from the date they reach the target offering amount.[432] For issuers accepting proceeds in excess of the target offering amount, this requirement will be triggered five days after the offering deadline.[433] We believe that requiring a report of the total amount of securities sold in the offering is necessary to inform investors about the ultimate size of the offering, especially in cases where an issuer may have sold more than the target offering amount. Further, this requirement will result in a central repository of this information at the Commission – information that otherwise might no longer be available on the intermediary's platform after the offering terminated. Finally, we note that requiring a final report will make data available to the Commission and the general public that could be used to evaluate the effects of the Section 4(a)(6) exemption on capital formation.

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432 *See* Rule 203(a)(3)(i) of Regulation Crowdfunding.

433 *See* Rule 203(a)(3)(ii) of Regulation Crowdfunding.

c. Amendments to the Offering Statement

(1) Proposed Rules

Proposed Rule 203(a)(2) of Regulation Crowdfunding would require that an issuer amend its disclosure for any material change in the offer terms or disclosure previously provided to investors. The amended disclosure would be filed with the Commission on Form C-A: Amendment and provided to investors and the relevant intermediary. Material changes would require reconfirmation by investors of their investment commitments within five business days. In addition, an issuer would be permitted, but not required, to file amendments for changes that are not material.

(2) Comments Received on Proposed Rules

Commenters were mixed on the proposed rules relating to amendments to the offering statement, with those opposed citing the burden on issuers.[434] Some commenters recommended that the Commission specify a filing deadline for amendments reflecting a material change,[435] and some recommended we require that investors be notified of the amendment.[436] Two commenters supported our view that the establishment of the final price should be considered a material change that would always require an amendment to Form C,[437] while one commenter opposed

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434 For commenters generally in support, *see, e.g.*, CFA Institute Letter; CrowdCheck Letter 1 (recommending that only a final amendment prior to the offering deadline be required, provided there is a five day reconfirmation period between filing and the sale of securities); EMKF Letter; Wefunder Letter.

For commenters generally opposed, *see, e.g.*, ASSOB Letter (suggesting a supplement could suffice in certain instances); Public Startup Letter 2; RocketHub Letter (suggesting that not all amendments be filed with the Commission so long as the information was made available through the intermediary).

435 *See, e.g.*, Commonwealth of Massachusetts Letter; Grassi Letter; Hackers/Founders Letter; RocketHub Letter.

436 *See, e.g.*, Arctic Island Letter 5; CFA Institute Letter; Grassi Letter; Joinvestor Letter; RoC Letter; RocketHub Letter. *But see* Public Startup Letter 2.

437 *See* Grassi Letter (recommending that reconfirmation not be required if the initial price is established in the offering documents and does not vary more than within a reasonable range established in such documents); Joinvestor Letter.

such an approach.[438] One commenter recommended that the Commission define "material change" in this context.[439]

(3) Final Rules

We are adopting requirements for the amendment to the offering statement as proposed. The final rules require that an issuer amend its disclosure for any material change in the offer terms or disclosure previously provided to investors.[440] While we recognize commenters' concerns about the costs that requiring one or more additional filings may impose on issuers, we note that an amendment will be required only in instances in which there was a material change. In such circumstances, we believe the additional efforts required of an issuer to file an amendment will be justified in order to provide investors with the information they need to make an informed investment decision.

The amended disclosure must be filed with the Commission on Form C and provided to investors and the relevant intermediary. Under the final rules, the issuer is required to check the box for "Form C/A: Amendment" on the cover of the Form C and explain, in summary manner, the nature of the changes, additions or updates in the space provided.[441]

With respect to what constitutes a "material change," as we stated in the Proposing Release, information is material if there is a substantial likelihood that a reasonable investor would consider it important in deciding whether or not to purchase the securities.[442] For example,

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438 *See* Public Startup Letter 2.

439 *See* ODS Letter.

440 *See* Rule 203(a)(2) of Regulation Crowdfunding. *See also* Section II.C.6 for discussion of the requirement that investors reconfirm their investment commitments following a material change.

441 *See* Form C.

442 See Basic Inc. v. Levinson, 485 U.S. 224 (1988) (quoting TSC Indus., Inc. v. Northway, Inc., 426 U.S. 438 (1976)).

we believe that a material change in the financial condition or the intended use of proceeds requires an amendment to an issuer's disclosure. Also, in those instances in which an issuer has previously disclosed only the method for determining the price, and not the final price, of the securities offered, we believe that determination of the final price is a material change to the terms of the offer and must be disclosed. These are not, however, the only possible material changes that require amended disclosure. We are not providing additional guidance on what constitutes a "material change," as requested by one commenter,[443] because, consistent with our historical approach to materiality determinations, we believe that an issuer should determine whether changes in the offer terms or disclosure are material based on the facts and circumstances.

In addition, as discussed further in Section II.C.6 below, if any change, addition or update constitutes a material change to information previously disclosed, the issuer must check the box on the cover of Form C indicating that investors must reconfirm their investment commitments.

A number of commenters recommended that we specify a filing deadline for amendments reflecting a material change,[444] and that we require investors be notified in some manner of the amendment.[445] We are not, however, amending the requirement as suggested by those commenters. We appreciate the need for investors to know this information in a timely fashion, but we believe that with the requirement that investors reconfirm their commitments, it will be in an issuer's interest to file an amendment as soon as practicable and to notify investors so that it

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443 *See* ODS Letter.

444 *See, e.g.*, Commonwealth of Massachusetts Letter; Grassi Letter; Hackers/Founders Letter; RocketHub Letter.

445 *See, e.g.*, Arctic Island Letter 5; CFA Institute Letter; Grassi Letter; Joinvestor Letter; RoC Letter; RocketHub Letter. *But see* Public Startup Letter 2.

will be in a position to close the offering. Therefore, we do not believe further procedural requirements are necessary.

Issuers will be permitted, but not required, to amend the Form C to provide information with respect to other changes that are made to the information presented on the intermediary's platform and provided to investors.[446] If an issuer amends the Form C to provide such information, it is not required to check the box indicating that investors must reconfirm their investment commitments.

2. Ongoing Reporting Requirements

a. Proposed Rules

Securities Act Section 4A(b)(4) requires, "not less than annually, [the issuer to] file with the Commission and provide to investors reports of the results of operations and financial statements of the issuer, as the Commission shall, by rule, determine appropriate, subject to such exceptions and termination dates as the Commission may establish, by rule."

To implement the ongoing reporting requirement in Section 4A(b)(4), we proposed in Rules 202 and 203 of Regulation Crowdfunding to require an issuer that sold securities in reliance on Section 4(a)(6) to file a report annually, no later than 120 days after the end of the most recently completed fiscal year covered by the report. To implement the requirement that issuers provide the report to investors, we proposed in Rule 202(a) to require issuers to post the annual report on their websites. Under proposed Rule 202(a), the issuer would be required to disclose information similar to that required in the offering statement, including disclosure about its financial condition that meets the highest financial statement requirements that were applicable to its offering statement.

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[446] *See* Instruction to paragraph (a)(2) of Rule 203 of Regulation Crowdfunding.

We also proposed in Rule 202(b) to require issuers to file the annual report until one of the following events occurs: (1) the issuer becomes a reporting company required to file reports under Exchange Act Sections 13(a) or 15(d); (2) the issuer or another party purchases or repurchases all of the securities issued pursuant to Section 4(a)(6), including any payment in full of debt securities or any complete redemption of redeemable securities; or (3) the issuer liquidates or dissolves in accordance with state law.

b. Comments on the Proposed Rules

Commenters expressed a range of views on the proposed ongoing reporting requirements.[447]

Frequency. With respect to frequency, a number of commenters supported the proposed requirement of annual reporting,[448] while a few recommended quarterly reporting.[449] Some commenters supported requiring issuers to file reports to disclose the occurrence of material events on an ongoing basis,[450] and several recommended that the Commission provide a list of

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447 For commenters generally supporting the proposed ongoing reporting requirements, *see, e.g.*, CfPA Letter; Commonwealth of Massachusetts Letter; Grassi Letter; Jacobson Letter; Leverage PR Letter; StartEngine Letter 1.

For commenters generally opposing the proposed ongoing reporting requirements, *see, e.g.*, ABA Letter; Campbell R. Letter; EMKF Letter; Guzik Letter 1; NFIB Letter; Public Startup Letter 2; RocketHub Letter; SeedInvest Letter 1; Stephenson, *et al* Letter.; Traklight Letter; WealthForge Letter; Winters Letter.

448 *See, e.g.*, AICPA Letter; CFIRA Letter 7; EY Letter; Grassi Letter; RoC Letter; RocketHub Letter; Traklight Letter.

449 *See, e.g.*, ASSOB Letter; CCI Letter; Denlinger Letter 1 (recommending quarterly reporting to provide investors and the secondary market timely information).

450 *See, e.g.*, ABA Letter (recommending amending Form C-AR within 15 calendar days of the material event); Angel Letter 1 (recommending prompt disclosure through postings on the issuer's website or social media); Denlinger Letter 1; EY Letter (recommending disclosure within 30 days of the end of the month in which the material event occurred, with such disclosure scaled for different tiers of issuers); Hackers/Founders Letter (recommending quarterly updates); RocketHub Letter (recommending quarterly updates).

events that would trigger such disclosure.[451] Two other commenters opposed such a requirement.[452]

Provision of Reports. Generally, commenters supported requiring issuers to post the annual report on their websites,[453] although some commenters favored a more limited distribution.[454] Similarly, a number of commenters supported requiring issuers to file the annual report on EDGAR,[455] while two commenters opposed such requirement.[456] In addition, most commenters opposed requiring physical delivery of the report directly to investors,[457] although some commenters supported requiring direct delivery in some form[458] or directly notifying investors of the availability of the annual report.[459]

Financial Statements. Commenters expressed differing views about the proposed ongoing financial statements requirements, particularly the level of public accountant involvement required. While a few supported requiring certain issuers to provide audited or reviewed financial

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451 *See, e.g.*, Denlinger Letter 1; EY Letter; Grassi Letter; RocketHub Letter.

452 *See* Heritage Letter; Public Startup Letter 2.

453 *See, e.g.*, ABA Letter; Angel Letter 1; CFA Institute Letter; Commonwealth of Massachusetts Letter; Grassi Letter; Jacobson Letter; Joinvestor Letter; RFPIA Letter; Traklight Letter.

454 *See, e.g.*, Crowdpassage Letter 3 (opposing the public availability of ongoing financial statements and recommending they be distributed through a password protected website accessible to investors); Frutkin Letter (recommending the annual report be provided to investors via e-mail, on a password-protected website accessible to investors or by mailing the report first-class to investors); Public Startup Letter 2.

455 *See, e.g.*, Commonwealth of Massachusetts Letter; Frutkin Letter; Grassi Letter; RocketHub Letter; Traklight Letter.

456 *See* Crowdpassage Letter 3 (opposing public availability of ongoing financial statements); Public Startup Letter 2.

457 *See, e.g.*, CFIRA Letter 7; CFIRA Letter 8; CfPA Letter; Crowdpassage Letter 3; Grassi Letter; Jacobson Letter; Public Startup Letter 2; Traklight Letter.

458 *See, e.g.*, Arctic Island Letter 5; CCI Letter; RocketHub Letter.

459 *See, e.g.*, Arctic Island Letter 5; CFA Institute Letter (recommending advance notice as to when and where annual reports will be available); RocketHub Letter.

statements on an ongoing basis,[460] a substantial number opposed an ongoing audit or review requirement.[461] Further, a number of commenters recommended that if ongoing financial statements are to be required for some issuers, the level of review be based on a higher offering amount threshold than the threshold used to determine the level of involvement of the accountant in the offering.[462]

Other Content. A number of commenters recommended that the ongoing annual reports require a more limited set of disclosure than the information required in the offering statement.[463]

Exceptions/Termination of Ongoing Reporting Requirement. A number of commenters recommended that there be exceptions to the ongoing reporting requirements for certain issuers,[464] expressing concern that the ongoing reporting obligations were too costly and could potentially extend indefinitely.[465] Others were opposed to such exceptions.[466]

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460 *See, e.g.*, ABA Letter; Denlinger Letter 1; Grassi Letter.

461 *See, e.g.*, AEO Letter; Arctic Island Letter 5; AWBC Letter; CrowdCheck Letter 4; EarlyShares Letter; EMKF Letter; Frutkin Letter; Graves Letter; Guzik Letter 1; iCrowd Letter; McGladrey Letter; Milken Institute Letter; NFIB Letter; PBA Letter; Peers Letter; RocketHub Letter; SeedInvest Letter 1; Seyfarth Letter; StartupValley Letter; Stephenson, *et al.* Letter; Traklight Letter; WealthForge Letter.

462 *See, e.g.*, Arctic Island Letter 5;CrowdCheck Letter 4; EarlyShares Letter; EY Letter; Grassi Letter; Graves Letter; iCrowd Letter; Milken Institute Letter; PBA Letter; Seyfarth Letter; Traklight Letter.

463 *See, e.g.*, EarlyShares Letter; EMKF Letter; McGladrey Letter; Milken Institute Letter; PBA Letter; RocketHub Letter.

464 *See, e.g.*, Heritage Letter (issuers raising $100,000 or less); RocketHub Letter (issuers raising $250,000 or less, although recommending that intermediaries be permitted to require ongoing reports on their platform even if exempted by the Commission); SeedInvest Letter 1 (recommending excepting issuers from ongoing reporting when: (1) raising less than $350,000; (2) securities are structured such that there can be no investment decisions; (3) an institutional investor, venture capitalist, or angel investor is leading the deal for investors; or (4) all investors have contractually waived the right to receive ongoing reports with informed consent); SeedInvest Letter 4. *See also* form letters designated as Type A (supporting SeedInvest Letter 1).

465 *See* SeedInvest Letter 1 (noting that the ongoing reporting obligations were an "obstacle to making crowdfunding a viable option for startups and small businesses" as the cost structure would be "out of proportion with the amounts proposed to be raised.")

466 *See, e.g.*, Commonwealth of Massachusetts Letter; Denlinger Letter 1; Grassi Letter; Public Startup Letter 2.

We also received a range of comments about when the ongoing reporting requirements should terminate, with two supporting requiring issuers to file an annual report until one of the enumerated events occurs,[467] and others suggesting alternatives to such requirement.[468]

Some commenters recommended that the ongoing reporting requirements be a condition to the Section 4(a)(6) exemption[469] while several others generally opposed such concept.[470]

c. Final Rules

After considering the comments received, we are adopting the ongoing reporting requirements generally as proposed, with a substantial modification to the level of public accountant involvement required and another modification to provide for termination of the ongoing reporting obligation in two additional circumstances.

Frequency. The final rules require an issuer that sold securities in reliance on Section 4(a)(6) to file an annual report with the Commission, no later than 120 days after the end of the fiscal year covered by the report.[471] We believe that this ongoing reporting requirement should benefit investors by enabling them to consider updated information about the issuer, thereby allowing them to make more informed investment decisions.

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467 *See, e.g.*, Grassi Letter; Whitaker Chalk Letter.

468 *See, e.g.*, ABA Letter; EY Letter (recommending the ongoing reporting obligations terminate after a certain amount of time if the issuer has 300 or fewer security holders); Grassi Letter; PBA Letter (recommending the reporting obligations terminate after three consecutive annual reports or after an issuer repurchases two-thirds of the outstanding securities issued in reliance on Section 4(a)(6), so long as the issuer made a bona fide offer to repurchase all of such securities); Public Startup Letter 2; RocketHub Letter (recommending the reporting obligations terminate after three annual reports).

469 *See, e.g.*, Parsont Letter (with a notice and cure provision); RocketHub Letter (recommending the ongoing reporting requirements be a condition for a minimum of three years).

470 *See, e.g.*, Public Startup Letter 2; Wefunder Letter; Whitaker Chalk Letter (recommending that (i) a condition, if any, apply only to the first annual report; (ii) that the failure to file the annual report restrict an issuer's ability to raise capital in the future; or (iii) issuers, certain officers, directors and shareholders have the option to escrow their shares for up to 24 months, with certain penalties for failure to file the annual report).

471 *See* Rule 202(a) of Regulation Crowdfunding.

We recognize the view of some commenters[472] that there may be major events that occur between annual reports about which investors would want to be updated, and we note that some commenters also recommended quarterly reporting. [473] However, we agree with those commenters[474] who said an annual requirement is sufficient. We believe a more frequent filing requirement would require an allocation of resources to the reporting function of Regulation Crowdfunding issuers that we do not believe is justified in light of the smaller amounts that will be raised pursuant to the exemption. We note that under Tier 1 of Regulation A, issuers can raise significantly more money – up to $20 million – without any ongoing reporting requirement other than to file a Form 1-Z exit report upon completion or termination of the offering. While not required, nothing in the rules prevents an issuer from updating investors when major events occur. Nor do our rules prevent intermediaries from requiring more frequent reporting. However, we do not believe that it is necessary in the final rules to require reporting on a more frequent basis than the annual ongoing reporting directly contemplated by the statute.

Provision of Reports. We also are adopting as proposed the requirement that an issuer post the annual report on its website.[475] Consistent with the proposal, the final rules do not require delivery of a physical copy of the annual report. As discussed in the Proposing Release and as supported by a number of commenters, we believe that investors in this type of Internet-based offering will be familiar with obtaining information on the Internet and that providing information

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472 *See, e.g.*, ABA Letter; Angel Letter 1; Denlinger Letter 1; EY Letter; Grassi Letter; Hackers/Founders Letter; RocketHub Letter.

473 *See, e.g.*, ASSOB Letter; CCI Letter; Denlinger Letter 1.

474 *See, e.g.*, AICPA Letter; CFIRA Letter 7; EY Letter; Grassi Letter; RoC Letter; RocketHub Letter; Traklight Letter.

475 *See* Rule 202(a) of Regulation Crowdfunding.

in this manner will be cost efficient. While some commenters[476] suggested that limiting distribution of the annual report to investors through use of a password-protected website would help protect an issuer's commercially-sensitive information, we believe such a requirement would add complexity for issuers and investors without providing significant protection of commercially-sensitive information since the reports could still be accessed by the public on EDGAR.

Consistent with the proposal, the final rule does not require an issuer to provide direct notification via e-mail or otherwise of the posting of the report, as was suggested by some commenters.[477] As discussed above in Section II.B.1.a.(i)(g), however, we are revising the final rules to require an issuer to disclose in the offering statement where on the issuer's website investors will be able to find the issuer's annual report and the date by which the annual report will be available on the issuer's website.[478] We believe these changes will help investors to locate the annual report. As discussed in the Proposing Release, we believe that many issuers may not have e-mail addresses for investors, especially after the shares issued pursuant to Section 4(a)(6) are traded by the original purchasers. Nonetheless, to the extent e-mail addresses for investors are available, an issuer could refer investors to the posted report via e-mail.

Financial Statements. After considering the comments, we are persuaded by the commenters that opposed requiring that an audit or review of the financial statements be included in the annual report.[479] Therefore, instead of requiring financial statements in the annual report

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476 *See, e.g.*, Crowdpassage Letter 3; Frutkin Letter.

477 *See, e.g.*, Arctic Island Letter 5 (intermediary should notify); Frutkin Letter; RocketHub Letter.

478 *See* Rule 201(w) of Regulation Crowdfunding.

479 *See, e.g.*, AEO Letter; Arctic Island Letter 5; AWBC Letter; CrowdCheck Letter 4 ("ongoing audit requirement will create an unpredictable on-going burden"); EarlyShares Letter; EMKF Letter ("audited financial statements, particularly for ongoing reporting requirements, are so cost-prohibitive for startups that

that meet the highest standard previously provided, the final rules require financial statements of the issuer certified by the principal executive officer of the issuer to be true and complete in all material respects.[480] However, issuers that have available financial statements that have been reviewed or audited by an independent certified public accountant because they prepare them for other purposes must provide them and will not be required to have the principal executive officer certification.[481]

Many commenters expressed concerns with the costs associated with preparing reviewed and audited financial statements on an ongoing basis. Commenters also noted the absence of comparable ongoing reporting requirements under Tier 1 of Regulation A and other offering exemptions.[482] While we recognize that Regulation Crowdfunding is different in many respects from Regulation A, we believe that crowdfunding issuers should not have more onerous ongoing reporting compliance costs than issuers that use another public offering exemption that permits higher maximum offering amounts. The changes to the ongoing reporting requirements in the rules we are adopting today will alleviate some of the costs on crowdfunding issuers. At the same time, we also believe, consistent with the views of at least one commenter,[483] that investors still

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they make absolutely no sense as an appropriate use of funds."); Frutkin Letter; Graves Letter; Guzik Letter 1; iCrowd Letter; McGladrey Letter; Milken Institute Letter; NFIB Letter; PBA Letter; Peers Letter; RocketHub Letter; SeedInvest Letter 1; Seyfarth Letter; StartupValley Letter; Stephenson, *et al.* Letter; Traklight Letter; WealthForge Letter.

480 *See* Rule 202(a) of Regulation Crowdfunding.

481 *Id*.

482 *See, e.g.*, CrowdCheck Letter 4; EMKF Letter; EY Letter;

483 *See* CrowdCheck Letter 4 ("While the on-going audit requirement is designed to provide investors and potential secondary purchasers of the company's securities with updated information about the company, it is unnecessary given the other, less burdensome, on-going disclosure requirements contained in the statute and proposed regulation.").

will be provided with sufficient ongoing financial information about the issuer under the final rules.

Other Content. With the exception of the financial statement requirement described above, the final rule adopts as proposed the requirement that the annual report include the information required in the offering statement. Although an issuer will not be required to provide the offering-specific information that it filed at the time of the offering (because the issuer will not be offering or selling securities),[484] it will be required to disclose information about the company and its financial condition, as required in connection with the offer and sale of the securities.[485] While we appreciate the recommendations of commenters for a more limited set of disclosure in the annual report, we believe that the disclosure costs of ongoing reporting for issuers will be less than in the initial offering statement, because they will be able to use the offering materials as a basis to prepare the annual reports. We believe investors will benefit from the availability of annual updates to the information they received when making the decision to invest in the issuer's securities, since these updates will allow them to be informed about issuer developments as they decide whether to continue to hold or sell, or how to vote, the securities. Under the statute and the final rules, the securities will be freely tradable after one year. Therefore, this information also

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484 *See* Rule 202(a) of Regulation Crowdfunding. An issuer will not be required to provide information about: (1) the stated purpose and intended use of the proceeds of the offering; (2) the target offering amount and the deadline to reach the target offering amount; (3) whether the issuer will accept investments in excess of the target offering amount; (4) whether, in the event that the offer is oversubscribed, shares will be allocated on a pro-rata basis, first come-first served basis, or other basis; (5) the process to complete the transaction or cancel an investment commitment once the target amount is met; (6) the price to the public of the securities being offered; (7) the terms of the securities being offered; (8) the name, SEC file number and CRD number (as applicable) of the intermediary through which the offering is being conducted; and (9) the amount of compensation paid to the intermediary.

485 *See* Rule 202(a) of Regulation Crowdfunding. Issuers will be required to provide disclosure about its directors and officers, business, current number of employees, financial condition (including financial statements), capital structure, significant factors that make an investment in the issuer speculative or risky, material indebtedness and certain related-party transactions.

will benefit potential future holders of the issuer's securities and help them to make more informed investment decisions.

Exceptions/Termination of Ongoing Reporting Requirement. After considering the comments, we are providing for termination of the ongoing reporting obligation in the three circumstances that we proposed as well as the following two additional circumstances: (1) when the issuer has filed at least one annual report and has fewer than 300 holders of record; and (2) when the issuer has filed at least three annual reports and has total assets that do not exceed $10 million. Accordingly, under Rule 202(b), issuers will be required to file the annual report until the earliest of the following events occurs:

(1) the issuer is required to file reports under Exchange Act Sections 13(a) or 15(d);

(2) the issuer has filed at least one annual report and has fewer than 300 holders of record;

(3) the issuer has filed at least three annual reports and has total assets that do not exceed $10 million;

(4) the issuer or another party purchases or repurchases all of the securities issued pursuant to Section 4(a)(6), including any payment in full of debt securities or any complete redemption of redeemable securities; or

(5) the issuer liquidates or dissolves in accordance with state law.

We believe the addition of the two termination events, which are generally consistent with the suggestions of commenters,[486] should help alleviate commenters' concerns about related costs for certain issuers that may not have achieved a level of financial success that would sustain an ongoing reporting obligation. The 300 shareholder threshold reflected in Rule 202(b)(2) is

[486] *See, e.g.*, ABA Letter; EY Letter (recommending the reporting obligations terminate after a certain amount of time if the issuer has 300 or fewer security holders); PBA Letter; RocketHub Letter (recommending the reporting obligations terminate after three consecutive annual reports).

consistent with the threshold used to determine whether an Exchange Act reporting company is eligible to suspend its Section 15(d)[487] or terminate its Section 13[488] reporting obligations. The option for an issuer to conclude ongoing reporting after three annual reports as reflected in Rule 202(b)(3) should help address concerns raised by some commenters that the reporting obligation could potentially extend indefinitely, while still requiring larger issuers with more than $10 million in total assets to continue reporting. We chose the $10 million threshold in order to be consistent with the total asset threshold in Section 12(g)(1) of the Exchange Act.[489] Under that provision, a company that has total assets exceeding $10 million and a class of securities held of record by a certain number of persons must register that class of securities with the Commission.

As proposed, Rule 203(b)(3) provides that any issuer terminating its annual reporting obligations will be required to file with the Commission, within five business days from the date on which the issuer becomes eligible to terminate its reporting obligation, a notice that it will no longer file and provide annual reports pursuant to the requirements of Regulation Crowdfunding. The issuer also must check the box for "Form C-TR: Termination of Reporting" on the cover of Form C. [490]

We are not persuaded by the suggestion of one commenter[491] that ongoing reports should be a condition to the Section 4(a)(6) exemption. As two commenters noted at the pre-proposal stage, under such an approach, compliance with the exemption would not be known at the time of

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487 *See* 17 CFR 240.12h-3.

l488 15 U.S.C. 78m.

489 15 U.S.C. 78*l*(g)(1).

490 *See* cover page of Form C.

491 *See* Parsont Letter

the transaction.[492] This, in turn, would create substantial uncertainty for issuers because there would be an indefinite possibility of a potential future violation of the exemption. We have modified the final rules from the proposal to clarify that the availability of the crowdfunding exemption is not conditioned on compliance with the annual reporting, progress update or termination of reporting obligations.[493] Nevertheless, issuers offering and selling securities in reliance on Section 4(a)(6) remain obligated to comply with these reporting requirements. Moreover, as discussed in Section II.A.4 above, the final rules deny issuers the benefit of relying on the exemption under Section 4(a)(6) for future offerings until they file, to the extent required, the two most recently required annual reports.[494] In addition, the final rules require the issuer to disclose in its offering statement and annual report if it, or any of its predecessors, previously failed to comply with the ongoing reporting requirements of Regulation Crowdfunding.

3. Form C and Filing Requirements

a. Proposed Rules

Securities Act Section 4A(b)(1) requires issuers who offer or sell securities in reliance on Section 4(a)(6) to "file with the Commission and provide to investors and the relevant broker or funding portal, and make available to potential investors" certain disclosures. The statute does not specify a format that issuers must use to present the required disclosures and file these disclosures with the Commission. We proposed in Rule 203 of Regulation Crowdfunding to require issuers to file the mandated disclosure using new Form C, which would require certain disclosures to be

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492 *See* Letter from Andrea L. Seidt, Comm'r, Ohio Div. of Sec. *available at* http://www.sec.gov/comments/jobs-title-iii/jobstitleiii-199.pdf; Letter from John R. Fahy, Partner, Whitaker Chalk Swindle Schwartz, *available at* http://www.sec.gov/comments/jobs-title-iii/jobstitleiii-175.htm.

493 *See* Rule 100(b)(4) of Regulation Crowdfunding.

494 *See* Rule 100(b)(5) of Regulation Crowdfunding.

presented in a specified format, while allowing the issuer to customize the presentation of other disclosures required by Section 4A(b)(1) and the related rules.

We proposed to require issuers to use an XML-based fillable form to input certain information. Information not required to be provided in text boxes in the XML-based fillable form would be filed as attachments to Form C.

Under the proposed rules, Form C would be used for all of an issuer's filings with the Commission related to the offering made in reliance on Section 4(a)(6). The issuer would check one of the following boxes on the cover of the Form C to indicate the purpose of the Form C filing:

- "Form C: Offering Statement" for issuers filing the initial disclosures required for an offering made in reliance on Section 4(a)(6);
- "Form C-A: Amendment" for issuers seeking to amend a previously-filed Form C for an offering;
- "Form C-U: Progress Update" for issuers filing a progress update required by Section 4A(b)(1)(H) and the related rules;
- "Form C-AR: Annual Report" for issuers filing the annual report required by Section 4A(b)(4) and the related rules; and
- "Form C-TR: Termination of Reporting" for issuers terminating their reporting obligations pursuant to Section 4A(b)(4) and the related rules.

EDGAR would automatically provide each filing with an appropriate tag depending on which box the issuer checks so that investors could distinguish among the different filings.[495]

Section 4A(b)(1) requires issuers to file the offering information with the Commission, provide it to investors and the relevant intermediary and make it available to potential investors.[496] Under the proposed rules, issuers would satisfy the requirement to file the information with the Commission by filing the Form C: Offering Statement, including any amendments and progress updates, on EDGAR. To satisfy the requirement to provide the disclosures to the relevant intermediary, we proposed that issuers provide to the relevant intermediary a copy of the disclosures filed with the Commission. To satisfy the requirement to provide the disclosures, or make them available, as applicable, to investors, we proposed that issuers provide the information to investors electronically by referring investors, such as through a posting on the issuer's website or by e-mail, to the information on the intermediary's platform. The proposed rules would not require issuers to provide physical copies of the information to investors.

b. Comments on the Proposed Rules

Commenters generally supported the proposed Form C requirement.[497] Two commenters supported the proposal to use one form with different EDGAR tags for each type of filing,[498] while another commenter recommended creating multiple forms in order to minimize the length

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495 EDGAR would tag the offering statement as "Form C," any amendments to the offering statement as "Form C-A," progress updates as "Form C-U," annual reports as "Form C-AR" and termination reports as "Form C-TR."

496 Section 4A(b)(4) requires issuers to file with the Commission and provide to investors, not less than annually, reports of the results of operations and financial statements of the issuer. As discussed above in Section II.B.2, to satisfy this requirement, the rules require an issuer to post the annual report on its website and file it with the Commission.

497 *See, e.g.*, Angel Letter 1 (specifically supporting the XML requirements); CFIRA Letter 7; Consumer Federation Letter; Grassi Letter; Hackers/Founders Letter; Traklight Letter; RocketHub Letter.

498 *See* Grassi Letter; RocketHub Letter.

of the form.[499] Two commenters recommended that the Commission modify Form C and its variants to require an issuer to indicate the jurisdictions in which the securities will be or are sold, with one of those commenters recommending ongoing disclosure of the amount sold in each state.[500]

Commenters were divided on the EDGAR filing requirement. Some commenters supported the filing requirement, with a few of those specifically supporting the proposal that issuers file the Form C in electronic format only.[501] Some commenters generally opposed the filing requirements or opposed specific aspects of the requirements.[502]

A few commenters requested clarification whether all offering material made available on the intermediary's platform must be filed on Form C.[503] Two commenters recommended that not all materials be required to be filed as exhibits.[504] A number of commenters noted that issuers would likely use various types of media for their offerings, some of which cannot be filed on

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499 *See* CFIRA Letter 7.

500 *See*, Commonwealth of Massachusetts Letter (recommending Form C require an issuer to check boxes indicating the jurisdictions in which securities will be sold); NASAA Letter (recommending Form C-U (offering update form) and Form C-AR (annual report form) require disclosure of the states where interests in the offering have been sold and the amount sold in each state).

501 For commenters supporting the EDGAR filings requirement generally, *see, e.g.*, CFIRA Letter 7; Traklight Letter. For those specifically supporting the electronic filing proposal, *see, e.g.*, Arctic Island Letter 5; CFIRA Letter 7; RocketHub Letter; Wilson Letter.

502 *See, e.g.*, Angel Letter 1; CFIRA Letter 1; CrowdCheck Letter 1; Mollick Letter; Public Startup Letter 2; RocketHub Letter; WealthForge Letter (recommending that the Commission require the filing of a Form C within 15 days of the offering first receiving an investment and at the completion of the offering).

503 *See, e.g.*, CrowdCheck Letter 1; Grassi Letter; Stephenson Letter.

504 *See, e.g.*, CFIRA Letter 1 (recommending that only "those documents most suited to police against fraud" be filed with the Commission because the intermediary serves as the primary repository of the offering materials); CrowdCheck Letter 1 (recommending the Commission permit issuers to use "free writing" disclosure materials in certain circumstances without having to file them with the Commission).

EDGAR.[505] A number of commenters recommended that the Commission adopt other disclosure formats, such as a question-and-answer format.[506]

A number of commenters generally supported the proposal to refer investors to information on the intermediary's platform.[507] With respect to the proposed methods (website posting or e-mail), one commenter stated that issuers would not have investors' e-mail addresses,[508] and another commenter noted that maintaining investors' email addresses would require significant resources.[509]

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505 *See, e.g.*, CFIRA Letter 6; CFIRA Letter 7; CrowdCheck Letter 1; Grassi Letter; Hackers/Founders Letter; RocketHub Letter; Wefunder Letter; Wilson Letter.

506 *See, e.g.*, Guzik Letter 1; Guzik Letter 2; Guzik Letter 3 (encouraging the Commission to provide an optional simplified disclosure format, perhaps in a question and answer format); Hackers/Founders Letter (encouraging the Commission to require a standard format and to allow issuers to provide additional information); Hamilton Letter (suggesting the Commission provide prototypes of Form C and sample disclosures); RocketHub (seeking a simple, standardized general form other than U-7 or A-1 to provide legal certainty); Saunders Letter (proposing that Form C be completed by selecting from a database of stock responses); SBA Office of Advocacy Letter (describing recommendations from its roundtable attendees to adopt a simple question and answer format similar to that previously used in Regulation A or to provide "standard boilerplate disclosures for some of the more complicated nonfinancial disclosures, such as risk factors," that are not required by the JOBS Act).

We also received several comments prior to the Proposing Release on whether the Commission should require a specific format for the required disclosure. Several commenters recommended that the Commission require the disclosure on a form modeled after, or require the use of NASAA's Small Company Offering Registration Form (U-7). *See, e.g.*, Coan Letter; Liles Letter 1; Vim Funding Letter; NASAA Letter. One commenter suggested modeling the required disclosure format after then-current Form 1-A, which is used for securities offerings made pursuant to Regulation A, but which has since been modified as a result of recently adopted amendments to Regulation A. *See* 17 CFR 230.251 et seq.; *Amendments to Regulation A*, Release No. 33-9741 (March 25, 2015) [80 FR 21805 (April 20, 2015)] Regulation A Adopting Release"); Commonwealth of Massachusetts Letter

507 *See, e.g.*, Grassi Letter; Joinvestor Letter; PeoplePowerFund Letter; Public Startup Letter 2; Wefunder Letter; Wilson Letter.

508 *See* Wefunder Letter.

509 *See* Grassi Letter.

c. Final Rules

We are adopting Form C and the related filing requirements[510] with a few modifications from the proposed rules.[511]

First, the final rules will amend Regulation S-T to permit an issuer to submit exhibits to Form C in Portable Document Format ("PDF") as official filings.[512] We appreciate the views of commenters that issuers would likely use various types of media for their offerings,[513] and believe that permitting these materials to be filed in PDF format will allow for more diverse presentations of information to be reasonably available to investors through a standardized, commonly available media. Under the final rules, issuers may customize the presentation of their non-XML disclosures and file those disclosures as exhibits to the Form C. For example, an issuer may provide the required disclosures by uploading to EDGAR, as an exhibit to Form C, a PDF version of the relevant information presented on the intermediary's platform, including charts, graphs, and a transcript or description of any video presentation or any other media not reflected in the PDF.

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510 An issuer that does not already have EDGAR filing codes, and to which the Commission has not previously assigned a user identification number, which we call a "Central Index Key (CIK)" code, will need to obtain the codes by filing electronically a Form ID [17 CFR 239.63; 249.446; 269.7 and 274.402] at https://www.filermanagement.edgarfiling.sec.gov. The applicant also will be required to submit a notarized authenticating document as a Portable Document Format (PDF) attachment to the electronic filing. The authenticating document will need to be manually signed by the applicant over the applicant's typed signature, to include the information contained in the Form ID and to confirm the authenticity of the Form ID. *See* 17 CFR 232.10(b)(2).

511 *See* Rule 203 of Regulation Crowdfunding. We have made some technical changes in the final rules that do not affect their substantive requirements. To maintain consistency with other Commission rules and to keep electronic filing requirements consolidated in Regulation S-T, we have deleted from proposed Rules 201, 202 and 203 the phrase "on EDGAR" where it appeared after "file with the Commission." We also have deleted the instruction to proposed Rule 203(a)(1) as the list of information set forth in that instruction was duplicative of the XML-based portion of Form C itself.

512 *See* Rule 101(a)(1)(xvii) of Regulation S-T. Regulation S-T generally allows PDF documents to be filed only as unofficial copies. *See* Rule 104 of Regulation S-T. However, Rule 101 provides for certain exceptions to this restriction. *See, e.g.*, Rule 101(ix)(allowing a PDF attachment to Form ID); Rule 101(a)(xiv)(requiring the filing of Form NRSRO and related exhibits in PDF as official filings).

513 *See, e.g.*, CFIRA Letter 6; CFIRA Letter 7; CrowdCheck Letter 1; Grassi Letter; Hackers/Founders Letter; RocketHub Letter; Wefunder Letter; Wilson Letter.

This approach should provide key offering information in a standardized format and give issuers flexibility in the presentation of other required disclosures. We believe this flexibility is important given that we expect that issuers engaged in offerings in reliance on Section 4(a)(6) would encompass a wide variety of industries at different stages of business development.

We are adopting the XML-based fillable form as proposed with a few modifications.[514] As suggested by some commenters,[515] the XML-based portion of Form C will require issuers to indicate by checkbox the jurisdictions in which securities are intended to be offered. We also are changing the name of proposed Form C-A to Form C/A to be consistent with the naming convention of our other amendment forms and adding Form C-AR/A to allow, and facilitate identification of, the amendment of an issuer's Form C-AR annual report. In addition, we are adding an instruction to clarify that the issuer should mark the appropriate box on the cover of Form C to indicate which form it is filing. We also are splitting the "Form, jurisdiction and date of organization" field into three fields to facilitate more accurate tracking of this data. We also inserted the statement required by paragraph (g) of Rule 201 immediately following the data required by that paragraph, so that statement appears together with the relevant data. Finally, we are modifying certain other field names and the General Instructions to Form C to clarify them or to reflect applicable changes to the disclosure requirements discussed above.

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514 As discussed in Section II.B.1, issuers will input in the proposed XML-based filing the following information: name, legal status and contact information of the issuer; name, SEC file number and CRD number (as applicable) of the intermediary through which the offering will be conducted; the amount of compensation paid to the intermediary to conduct the offering, including the amount of referral and other fees associated with the offering; any other direct or indirect interest in the issuer held by the intermediary, or any arrangement for the intermediary to acquire such an interest; number of securities offered; offering price; target offering amount; whether oversubscriptions will be accepted and, if so, how they will be allocated; maximum offering amount (if different from the target offering amount); deadline to reach the target offering amount; current number of employees of the issuer; selected financial data for the prior two fiscal years; and the jurisdictions in which the issuer intends to offer the securities.

515 *See, e.g.*, Commonwealth of Massachusetts Letter; NASAA Letter.

We believe that requiring certain information to be submitted in XML format will support the assembly and transmission of those required disclosures to EDGAR on Form C.[516] It also will make certain key information about each offering available to investors and market observers in electronic format and allow the Commission to observe the implementation of the crowdfunding exemption under Section 4(a)(6). Information will be available about the types of issuers using the exemption, including the issuers' size, location, securities offered and offering amounts and the intermediaries through which the offerings are taking place. We believe the addition of the requirement to indicate the jurisdictions in which the issuer intends to offer the securities, as suggested by several commenters, will facilitate oversight by state regulators, who retain antifraud authority over crowdfunding transactions, while imposing only minimal costs on issuers.

In addition, in a change from the proposed rules, the final Form C includes an optional Question and Answer ("Q&A") format that issuers may elect to use to provide the disclosures that are not required to be filed in XML format.[517] Issuers opting to use this format would prepare their disclosures by answering the questions provided and filing that disclosure as an exhibit to the Form C. A number of commenters noted that an optional format such as this would be less burdensome for small issuers while still providing the Commission and investors with the required information.[518] We believe that this option may help to facilitate compliance and ease burdens on by providing a mechanism by which issuers can easily confirm that they have provided all required information.

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516 The Commission will make the information available via EDGAR both in a traditional text-based format for reading and as downloadable XML-tagged data for analysis.

517 *See* Item 1 of General Instruction III to Form C of Regulation Crowdfunding.

518 *See, e.g.*, Guzik Letter 1; Guzik Letter 2; Guzik Letter 3; Hackers/Founders Letter; Hamilton Letter; RocketHub Letter; Saunders Letter; SBA Office of Advocacy Letter.

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Consistent with the proposal, we are adopting a single Form C for all filings under Regulation Crowdfunding.[519] We believe that the use of one form will be more efficient than requiring multiple forms, will not result in unduly lengthy forms, and will simplify the filing process for issuers and their preparers. EDGAR will automatically provide each filing with an appropriate tag depending on which box the issuer checks so that investors can distinguish among the different filings.

We also are adopting, largely as proposed, the requirements to provide the offering information to investors and the relevant intermediary and make it available to potential investors under Section 4A(b)(1).[520] In addition, as discussed above in Section II.B., we moved the definition of "investor" from proposed Rule 300(c)(4) to Rule 100(d) to clarify that for purposes of all of Regulation Crowdfunding, "investor" includes any investor or any potential investor, as the context requires.[521] In connection with this clarifying change, we have deleted the phrase "and make available to potential investors" each time it appeared in the rule text to avoid redundancy.[522]

The final rules provide that issuers will satisfy the requirement to file the offering information with the Commission and provide it to the relevant intermediary by filing the Form C: Offering Statement and any amendments and progress updates and providing to the relevant intermediary a copy of the disclosures filed with the Commission.[523] The initial offering

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519 *See* Rule 203 of Regulation Crowdfunding.

520 *See* Rule 203(a) of Regulation Crowdfunding.

521 *See* Rule 100(d) of Regulation Crowdfunding.

522 *See* Rule 203(a) of Regulation Crowdfunding.

523 *See* Instructions 1 and 2 to paragraph (a) of Rule 203 of Regulation Crowdfunding. We anticipate that issuers seeking to engage in an offering in reliance on Section 4(a)(6) may likely work with an intermediary to prepare the disclosure that would be provided on the intermediary's platform and filed with the Commission.

statement should include all of the information that is provided on the intermediary's website.[524] We also are adopting as proposed the requirements to file with the Commission and provide, or make available, as applicable, to investors and the relevant intermediary an amendment to the offering statement to disclose any material changes, additions or updates to information provided to investors through the intermediary's platform.[525] Issuers may, but are not required to, file an amendment to reflect other changes, additions or updates to information provided to investors through the intermediary's platform that it considers not material.

To satisfy the requirement to provide the disclosures, or make them available, as applicable, to investors, the final rules allow issuers to provide the information to investors electronically by referring investors to the information on the intermediary's platform through a posting on the issuer's website or by e-mail.[526] As discussed in the proposal and noted by commenters, many issuers may not have e-mail addresses for investors. Accordingly, the final rules permit issuers to provide this information to investors through a website posting.[527] However, to the extent e-mail addresses for investors are available to issuers, issuers may contact investors via e-mail to direct them to the posted information. We continue to believe that investors in this type of Internet-based offering will be familiar with obtaining information on the Internet and that providing the information in this manner will be cost-effective for issuers. As discussed in the Proposing Release, we believe Congress contemplated that crowdfunding would, by its very nature, occur over the Internet or other similar electronic media

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In some cases, intermediaries may offer, as part of their service, to file the disclosure with the Commission on behalf of the issuer.

524 *See* Rule 203(a)(1) of Regulation Crowdfunding.

525 *See* Rule 203(a)(2) of Regulation Crowdfunding.

526 *See* Instruction 2 to Rule 203(a) of Regulation Crowdfunding.

527 *See, e.g.*, Grassi Letter; Wefunder Letter.

that is accessible to the public.[528] Therefore, consistent with the proposed rules, the final rules do not require issuers to provide physical copies of the information to investors.

4. Prohibition on Advertising Terms of the Offering

a. Proposed Rules

Securities Act Section 4A(b)(2) provides that an issuer shall "not advertise the terms of the offering, except for notices which direct investors to the funding portal or broker." Consistent with the statute, proposed Rule 204 of Regulation Crowdfunding would allow an issuer to publish a notice advertising the terms of an offering in reliance on Section 4(a)(6) so long as the notice includes the address of the intermediary's platform on which additional information about the issuer and the offering may be found. The proposal did not impose limitations on how the issuer distributes the notices. As proposed, the notice could include no more than: (1) a statement that the issuer is conducting an offering, the name of the intermediary through which the offering is being conducted and a link directing the investor to the intermediary's platform; (2) the terms of the offering; and (3) factual information about the legal identity and business location of the issuer, limited to the name of the issuer of the security, the address, phone number and website of the issuer, the e-mail address of a representative of the issuer and a brief description of the business of the issuer. Under the proposed rules, "terms of the offering" would include: (1) the amount of securities offered; (2) the nature of the securities; (3) the price of the securities; and (4)

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528 We note that Section 301 of the JOBS Act states that "[Title III] may be cited as the 'Capital Raising Online While Deterring Fraud and Unethical Non-Disclosure Act of 2012'." *See* Section 301 of the JOBS Act. *See also* 158 Cong. Rec. S1689 (daily ed. March 15, 2012) (statement of Sen. Mark Warner) ("There is now the ability to use the Internet as a way for small investors to get the same kind of deals that up to this point only select investors have gotten…, where we can now use the power of the Internet, through a term called crowdfunding."); *id.* at S1717 (Statement of Sen. Mary Landrieu) ("this crowdfunding bill—which is, in essence, a way for the Internet to be used to raise capital…").

the closing date of the offering period. The proposed rules would not, however, restrict an issuer's ability to communicate other information that does not refer to the terms of the offering.

The proposed rules also would allow an issuer to communicate with investors about the terms of the offering through communication channels provided by the intermediary on the intermediary's platform, so long as the issuer identifies itself as the issuer in all communications.

b. Comments Received

Commenters were mostly supportive of these provisions. Several commenters expressed support for the proposed content of advertising notices[529] and the definition of "terms of the offering."[530] A number of commenters also supported the proposal's absence of a restriction on an issuer's ability to communicate information that does not refer to the terms of the offering.[531] Several commenters requested clarification on various aspects of the proposal.[532]

Several commenters recommended that, consistent with the proposal, the Commission not restrict the media or format that may be used for advertising notices,[533] with some pointing to the changing nature of social media and potential new user interfaces.[534] Two commenters, however, stated that communications about the offering should always be conducted through the intermediary.[535] A number of commenters also supported allowing an issuer to communicate with

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529 *See, e.g.*, CFIRA Letter 6; Commonwealth of Massachusetts Letter; RocketHub Letter.

530 *See, e.g.*, Arctic Island Letter 5; CFIRA Letter 6; Heritage Letter; Joinvestor Letter; RocketHub Letter.

531 *See, e.g.*, ABA Letter; CFIRA Letter 6; Consumer Federation Letter; Hackers/Founders Letter; Public Startup Letter 2; RocketHub Letter.

532 *See, e.g.*, ABA Letter (recommending the rule text include a safe harbor for regularly released factual business information so long as it does not refer to the terms of the offering); CIFRA Letter 6 (requesting more guidance on advertising formats and content and the definition of "terms of the offering").

533 *See, e.g.*, Arctic Island Letter 5; Joinvestor Letter; Public Startup Letter 2; RoC Letter; RocketHub Letter.

534 *See, e.g.*, Arctic Island Letter 5; Public Startup Letter 2; RocketHub Letter.

535 *See* Hackers/Founders Letter (supporting the issuer being able to repost the communications elsewhere so long as it first appeared through the intermediary); Joinvestor Letter.

investors about the terms of the offering through communication channels provided by the intermediary on the intermediary's platform, so long as the issuer identifies itself in all communications.[536]

Some commenters opposed the proposed advertising rules, with some stating that the advertising restrictions are unnecessary because sales must occur through an intermediary's platform, which would contain all of the relevant disclosures and investor acknowledgments.[537] One commenter asked that an issuer be given broader leeway to publicize its business or offering on its own website or social media platform so long as the specific terms of the offering can be found only through the intermediary's platform.[538] One commenter recommended allowing advertising notices to have a section for supplemental information highlighting certain intangible purposes such as a particular social cause.[539]

Two other commenters recommended that any advertising notices be filed with the Commission and/or the relevant intermediary.[540] Several other commenters supported the proposed approach of not having advertising notices filed with the Commission or the intermediary, citing concerns about various formats of the communications, inability to capture all third-party communications, and the costs associated with trying to capture the data.[541]

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536 *See, e.g.*, ASSOB Letter; CFIRA Letter 6; Commonwealth of Massachusetts Letter; Consumer Federation Letter; Hackers/Founders Letter; Odhner Letter; Public Startup Letter 2; RoC Letter; RocketHub Letter; Wefunder Letter. Some of these commenters also recommended that all interested persons, such as officers, directors and other agents, should identify themselves in all communications on the intermediary's platform. *See* CIFRA Letter 6; Hackers/Founders Letter.

537 *See, e.g.*, FundHub Letter 1; Seed&Spark Letter (noting the proposed advertising restrictions will restrict the ability of filmmakers to market and raise money for their films); Arctic Island Letter 5; PeoplePowerFund Letter.

538 *See* Fryer Letter.

539 *See* RocketHub Letter.

540 *See, e.g.*, Commonwealth of Massachusetts Letter; CFIRA Letter 6.

541 *See, e.g.*, Arctic Island Letter 5; ASSOB Letter; Public Startup Letter 2; RocketHub Letter.

c. Final Rules

We are adopting the prohibition on advertising terms of the offering substantially as proposed, with minor changes to the rule text for clarity.[542] Under the final rules, an advertising notice that includes the terms of the offering can include no more than: (1) a statement that the issuer is conducting an offering, the name of the intermediary through which the offering is being conducted and a link directing the investor to the intermediary's platform; (2) the terms of the offering; and (3) factual information about the legal identity and business location of the issuer, limited to the name of the issuer of the security, the address, phone number and website of the issuer, the e-mail address of a representative of the issuer and a brief description of the business of the issuer. Consistent with the proposal, the final rules define "terms of the offering" to include: (1) the amount of securities offered; (2) the nature of the securities; (3) the price of the securities; and (4) the closing date of the offering period.[543]

The permitted notices will be similar to "tombstone ads" under Securities Act Rule 134,[544] except that the notices will be required to direct an investor to the intermediary's platform through which the offering is being conducted, such as through a link directing the investor to the platform.

Although at least one commenter recommended allowing advertising notices to have a section for supplemental information highlighting certain intangible purposes such as a particular

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542 *See* Rule 204 of Regulation Crowdfunding.

543 *See* Instruction to Rule 204 of Regulation Crowdfunding.

544 17 CFR §230.134.

social cause,[545] we do not believe a separate section is necessary. Instead, this type of information may be included as part of the "brief description of the business."

Two commenters[546] expressed concern that the proposed rule would not allow enough flexibility for brief, informal social media communications, but we disagree. A notice cannot include more than the enumerated matters, but an issuer has the flexibility not to include each of the enumerated matters in the notice, which may facilitate certain types of social media communications. For example, an issuer would be able to note on its own website or on social media that it is conducting an offering and direct readers to the materials on the intermediary's platform. There is no requirement for legends on these notices because the issuer will be directing investors to the materials on the intermediary's platform that will include those required legends.

We believe that this approach will provide flexibility for issuers while protecting investors by limiting the advertising of the terms of the offering to the information permitted in the notice and directing them to the intermediary's platform where they can access the disclosures necessary for them to make informed investment decisions.

Consistent with the recommendation of several commenters,[547] the final rules do not impose limitations on how the issuer distributes the notices. For example, an issuer could place notices in newspapers or post notices on social media sites or the issuer's own website. We believe the final rules will allow issuers to leverage social media to attract investors, while at the same time protecting investors by limiting the ability of issuers to advertise the terms of the offering without directing them to the required disclosure. We are not adopting a requirement that

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545 *See* RocketHub Letter.

546 *See* FundHub Letter 1; Fryer Letter ("a rigid tombstone approach is inconsistent with the structure and informality of modern social media communication tools.")

547 *See, e.g.,* Arctic Island Letter 5; Joinvestor Letter; Public Startup Letter 2; RoC Letter; RocketHub Letter.

all notices be filed with the Commission or relevant intermediary, as requested by some commenters.[548] Other commenters expressed concerns about the costs that would be associated with such a requirement, and given that investors will be directed to the required disclosure on the intermediary's platform, we believe the final rules appropriately take these factors into account.[549]

Further, the final rules allow an issuer to communicate with investors about the terms of the offering through communication channels provided by the intermediary on the intermediary's platform, so long as the issuer identifies itself as the issuer in all communications. We believe that one of the central tenets of the concept of crowdfunding is that the members of the crowd decide whether or not to fund an idea or business after sharing information with each other. As part of those communications, we believe it is important for the issuer to be able to respond to questions about the terms of the offering or even challenge or refute statements made through the communication channels provided by the intermediary. Therefore, the final rules do not restrict issuers from participating in those communications so long as the issuer identifies itself as the issuer in all communications.

Based on the suggestion of a few commenters,[550] we are clarifying in the final rules that the prohibition on advertising the terms of the offering and related requirements apply to persons acting on behalf of the issuer.[551] For example, persons acting on behalf of the issuer are required under Rule 204(c) to identify their affiliation with the issuer in all communications on the intermediary's platform.[552]

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548 *See, e.g.*, Hackers/Founders Letter; Joinvestor Letter.

549 *See, e.g.*, ASSOB Letter; RocketHub Letter.

550 *See, e.g.*, CIFRA Letter 6; Hackers/Founders Letter.

551 *See* Rule 204 of Regulation Crowdfunding.

552 *See also* Section II.B.5 for disclosures required by persons promoting the offering.

In addition, the final rules do not restrict an issuer's ability to communicate other information that might occur in the ordinary course of its operations and that does not refer to the terms of the offering. As stated in the Proposing Release, we believe that this is consistent with the statute because Section 4A(b)(2) restricts the advertising of the terms of the offer. The Commission has interpreted the term "offer" broadly, however, and has explained that "the publication of information and publicity efforts, made in advance of a proposed financing which have the effect of conditioning the public mind or arousing public interest in the issuer or in its securities constitutes an offer…"[553] In this regard, we also note that Securities Act Rule 169[554] permits non-Exchange Act reporting issuers engaged in an initial public offering to continue to publish, subject to certain exclusions and conditions, regularly released factual business information that is intended for use by persons other than in their capacity as investors.

While one commenter requested a safe harbor for regularly released factual business information so long as it does not refer to the terms of the offering,[555] we do not believe that a safe harbor is necessary. Ultimately, whether or not a communication is limited to factual business information depends on the facts and circumstances of that particular communication. However, issuers may generally look to the provisions of Rule 169 for guidance in making this determination in the Regulation Crowdfunding context.

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553 *Securities Offering Reform*, Release No. 33-8591 (July 19, 2005) [70 FR 44722 (Aug. 3, 2005)] at 44731. The term "offer" has been interpreted broadly and goes beyond the common law concept of an offer. *See, e.g., Diskin v. Lomasney & Co*., 452 F.2d 871 (2d. Cir. 1971).

554 17 CFR 230.169.

555 *See* ABA Letter.

5. Compensation of Persons Promoting the Offering

a. Proposed Rules

Consistent with Securities Act Section 4A(b)(3), proposed Rule 205 of Regulation Crowdfunding would prohibit an issuer from compensating, or committing to compensate, directly or indirectly, any person to promote the issuer's offering through communication channels provided by the intermediary, unless the issuer takes reasonable steps to ensure that the person clearly discloses the receipt (both past and prospective) of compensation each time the person makes a promotional communication. Further, a founder or an employee of the issuer that engages in promotional activities on behalf of the issuer through the communication channels provided by the intermediary would be required to disclose, with each posting, that he or she is engaging in those activities on behalf of the issuer.

Under the proposed rules, an issuer would not be able to compensate or commit to compensate, directly or indirectly, any person to promote its offerings outside of the communication channels provided by the intermediary, unless the promotion is limited to notices that comply with the proposed advertising rules.

b. Comments Received

Commenters were generally supportive of promoter disclosure and the proposed rule.[556] A number of commenters supported the broad applicability of the proposed rules to persons acting

[556] *See, e.g.*, CFA Institute Letter; Consumer Federation Letter (supporting proposal but generally questioning the wisdom of allowing paid promoters to participate in the communication channels at all); NASAA Letter; NFIB Letter; Public Startup Letter 2.

on behalf of the issuer.[557] Some commenters recommended that the issuer or intermediary bear more responsibility for ensuring that the identity of the promoters be prominently disclosed.[558]

A number of commenters also supported the requirement in the proposal that an issuer not compensate or commit to compensate, directly or indirectly, any person to promote its offerings outside of the communication channels provided by the intermediary, unless the promotion is limited to notices that comply with the proposed advertising rules.[559]

c. Final Rules

We are adopting, as proposed, final rules about the compensation of persons promoting the offering, with one clarifying change.[560] We anticipate that communication channels provided by the intermediary will provide a forum through which investors could share information to help the members of the crowd decide whether or not to fund the issuer. We believe that it will be important for investors to know whether persons using those communication channels are persons acting on behalf of the issuer or persons receiving compensation from the issuer (or from persons acting on behalf of the issuer), to promote the issuer's offering because of the potential for self-interest or bias in communications by these persons.

A number of commenters supported the broad applicability of the proposed rules to persons acting on behalf of the issuer.[561] The text of the proposed rule included a sentence stating

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557 *See, e.g.*, CFA Institute Letter; CFIRA Letter 6; Commonwealth of Massachusetts Letter; Consumer Federation Letter; Hackers/Founders Letter; Joinvestor Letter; RocketHub Letter; MCS Letter.

558 *See, e.g.*, ASSOB Letter; Commonwealth of Massachusetts Letter; Joinvestor Letter; MCS Letter; RoC Letter; RocketHub Letter.

559 *See, e.g.*, ASSOB Letter; Consumer Federation Letter; Joinvestor Letter; Public Startup Letter 2; RoC Letter; RocketHub Letter.

560 *See* Rule 205 of Regulation Crowdfunding.

561 *See, e.g.*, CFA Institute Letter; CFIRA Letter 6; Commonwealth of Massachusetts Letter; Consumer Federation Letter; Hackers/Founders Letter; Joinvestor Letter; RocketHub Letter; MCS Letter.

that the disclosure obligation would apply to "a founder or an employee of the issuer that engages in promotional activities on behalf of the issuer through the communication channels." Based on comments received, we are removing that sentence and adding an instruction to clarify that the requirement applies broadly to all persons acting on behalf of the issuer, regardless of whether or not the compensation they receive is specifically for the promotional activities. The change is intended to clarify that the disclosure requirement applies to persons hired specifically to promote the offering as well as to persons (including, but not limited to, founders, employees and directors) who are otherwise employed by the issuer or who undertake promotional activities on behalf of the issuer.

While we appreciate the views of commenters who suggested that we impose additional requirements on issuers or intermediaries to ensure that the identity of promoters is prominently disclosed, we believe the requirement that the issuer take reasonable steps to ensure that promoters clearly disclose the receipt of compensation for communications is sufficient to achieve the objectives of this provision without being overly prescriptive. There are a number of reasonable steps the issuer can take to ensure compliance. An issuer could, for example, contractually require any promoter to include the required statement about receipt of compensation, confirm that the promoter is adhering to the intermediary's terms of use that require promoters to affirm whether or not they are compensated by the issuer, monitor communications made by such persons and take the necessary steps to have any communications that do not have the required statement removed promptly from the communication channels, or retain a person specifically identified by the intermediary to promote all issuers on its platform.

As proposed, the final rules also specify that the issuer shall not compensate or commit to compensate, directly or indirectly, any person to promote its offerings outside of the

communication channels provided by the intermediary, unless the promotion is limited to notices that comply with the advertising rules discussed above in Section II.B.4.[562] This prohibition should prevent issuers from circumventing the restrictions on advertising by compensating a third party to do what the issuer cannot do directly.

6. Other Issuer Requirements

a. Oversubscriptions

The proposed rules would not limit an issuer's ability to accept investments in excess of the target offering amount, subject to the $1 million annual limit.[563] Issuers would be required to disclose how much they would be willing to accept in oversubscriptions, how the oversubscriptions would be allocated, and the intended purpose of those additional funds.

Commenters were generally supportive of this approach to oversubscriptions.[564] Some commenters supported the proposed flexibility to allow issuers to determine how to allocate oversubscribed offerings, [565] while other commenters recommended that the Commission require issuers to allocate oversubscriptions using a prescribed method. [566] Two commenters recommended that the Commission limit the maximum oversubscription amount to a certain percentage of the target offering amount,[567] while two other commenters opposed such a limit.[568]

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562 *See* Rule 205(b) of Regulation Crowdfunding.

563 *See* proposed Rule 201(h) and Instruction to paragraph (i) of Rule 201 of Regulation Crowdfunding, and cover page of Form C.

564 *See, e.g.*, CFA Institute letter; EMKF letter; Jacobson letter; Wefunder letter.

565 *See, e.g.*, ASSOB Letter; CFA Institute Letter; EMKF Letter; Public Startup Letter 2; RocketHub Letter; Wefunder letter.

566 *See, e.g.*, Fund Democracy Letter (pro-rata); Consumer Federation Letter (same as Fund Democracy); Joinvestor letter (first-come, first-served or algorithmic random selection); PeoplePowerFund Letter (first-come, first-served).

567 *See* Joinvestor Letter (10%); RFPIA Letter (20%).

568 *See* Jacobson Letter; Public Startup Letter 2.

One commenter recommended that the Commission revise the proposed rules to clarify that issuers would be required to disclose the "other" basis upon which oversubscriptions would be allocated.[569]

We are adopting the rule relating to oversubscriptions as proposed, with one clarifying change.[570] We do not believe, as some commenters suggested, that it is necessary to limit the maximum oversubscription amount. Nor do we believe it is necessary to prescribe how to allocate oversubscribed offerings so long as the issuer discloses, at the commencement of the offering, how securities in such offerings will be allocated, and the intended purpose of those additional funds. This disclosure should provide investors with information they need to make informed investment decisions while providing issuers flexibility to structure the offering as they believe appropriate. In response to a comment received,[571] we are clarifying in the final rules that, regardless of the structure, the issuer must describe how securities in oversubscribed offerings will be allocated.

b. Offering Price

As discussed above in Section II.B.1.a.i.(e), proposed Rule 201(l) would require an issuer to disclose the offering price of the securities or, in the alternative, the method for determining the price, provided that prior to any sale of securities, each investor is provided in writing the final price and all required disclosure. The proposed rules would not require issuers to set a fixed price or prohibit dynamic pricing.

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569 *See* Fund Democracy Letter.

570 *See* Rule 201(h) to Regulation Crowdfunding.

571 *See* Fund Democracy Letter.

We received a few comments supporting the proposed approach or expressing opposition to requiring a fixed price,[572] while another commenter suggested the Commission require issuers to set a fixed price.[573]

We are adopting the final rules as proposed.[574] While we appreciate the view of at least one commenter[575] that a fixed price may be simpler for investors to understand, we believe that the statute contemplated flexible pricing by providing that issuers may disclose the method for determining the price, provided that the final price and required disclosures are provided to each investor prior to any sales. We also believe the cancellation rights in the final rules[576] will provide investors a reasonable opportunity to cancel their investment commitment if they wish to do so after the price is fixed.

c. Types of Securities Offered and Valuation

The proposed rules would not limit the type of securities that may be offered in reliance on Section 4(a)(6) nor prescribe a method for valuing the securities. Issuers would be required to describe the terms of the securities and the valuation method in their offering materials.

A number of commenters generally supported not limiting the types of securities that may be offered and sold in reliance of Section 4(a)(6).[577] Comments were more varied on valuation methodology. Some commenters recommended that the Commission neither require nor prohibit

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572 *See, e.g.*, CFA Institute Letter (stating that disclosure of changes and methods used to determine share prices, along with investors' rights to cancel their investment commitments, provide reasonable safeguards); Wilson Letter; Public Startup Letter 2.

573 *See* RocketHub Letter.

574 *See* Rule 201(l) of Regulation Crowdfunding. *See also* Section II.C.6 for a discussion of cancellation provisions.

575 *See* RocketHub Letter.

576 *See* Rules 201(j) and 201(k) of Regulation Crowdfunding.

577 *See, e.g.*, CFA Institute Letter; Concerned Capital Letter; Crowdstockz Letter; Hackers/Founders Letter; Joinvestor Letter; Public Startup Letter 2; RocketHub Letter; Tiny Cat Letter; Wilson Letter.

a specific valuation methodology,[578] while others recommended that the Commission prescribe a set of valuation standards that have universal application for startups.[579] Two commenters recommended that the Commission require issuers to base the valuation of their securities on the price at which the issuer previously sold securities,[580] and another commenter recommended that the Commission consider whether additional standards are needed to ensure that securities are fairly valued and that approaches to valuation that put investors at a disadvantage be prohibited.[581] One commenter generally supported requiring issuers to describe how securities being offered are being valued,[582] while another commenter generally opposed such requirement.[583]

We are adopting, as proposed, final rules that neither limit the type of securities that may be offered in reliance on Section 4(a)(6) nor prescribe a method for valuing the securities.[584] We noted in the proposal that the statute refers to "securities" and does not limit the type of securities that could be offered pursuant to the exemption. Issuers are required to describe the terms of the securities and the valuation method in their offering materials.[585] We believe this approach is consistent with the statute and will provide flexibility to issuers to determine the types of

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578 *See, e.g.*, Hackers/Founders Letter; Heritage Letter; PeoplePowerFund Letter; Public Startup Letter 2; RocketHub Letter; Wilson Letter.

579 *See, e.g.*, 11 Wells Letter; Active Agenda Letter; Borrell Letter; Ellenbogen Letter; Greer Letter; Mountain Hardwear Letter; Moyer Letter; NaviGantt Letter; Vidal Letter.

580 *See, e.g.*, Public Startup Letter 3; Wefunder Letter.

581 *See* Consumer Federation Letter.

582 *See* CFIRA Letter 7.

583 *See* Thomas Letter 2 (recommending that if issuers are required to describe the valuation method in their offering materials, the rule should provide "safe harbor" language that issuers can use in providing such description.)

584 *See* Rule 201(m) of Regulation Crowdfunding.

585 *See* Rule 201(m)(1) and (4) of Regulation Crowdfunding.

securities that they offer to investors and how those securities are valued, while providing investors with the information they need to make an informed investment decision.

While some commenters suggested that the Commission should provide specific valuation methods or standards for securities-based crowdfunding transactions, we are not persuaded that there would be sufficient benefits to being prescriptive in this regard. Methods and valuations of early stage companies vary significantly, and any attempt to choose a particular valuation methodology could limit flexibility and have the result of endorsing one approach over another without necessarily having a sound basis for doing so. We believe the requirement that issuers describe the methods they use to value their securities in their offering materials, including the requirement that they describe examples of methods for how such securities may be valued by the issuer in the future, will provide investors with the information they need to make an informed investment decision.

The final rules do not limit the types of securities that may be offered in reliance on Section 4(a)(6), and thus debt securities may be offered and sold in crowdfunding transactions. As we stated in the Proposing Release, in general, the issuance of a debt security raises questions about the applicability of the Trust Indenture Act of 1939 ("Trust Indenture Act").[586] Although the Trust Indenture Act applies to any debt security sold through the use of the mails or interstate commerce, including debt securities sold in transactions that are exempt from Securities Act registration, Trust Indenture Act Section 304(b) provides an exemption for any transaction that is exempted by Securities Act Section 4 from the provisions of Section 5 of the Act.[587] An issuer offering debt securities in reliance on Section 4(a)(6), therefore, would be able to rely on this

[586] 15 U.S.C. 77aaa *et seq*.

[587] 15 U.S.C. 77ddd(b).

exemption.[588] Based on the availability of this exemption, we are not adopting a specific exemption from the requirements of the Trust Indenture Act for offerings of debt securities made in reliance on Section 4(a)(6).

C. Intermediary Requirements

1. Definitions of Funding Portals and Associated Persons

a. Proposed Rules

Securities Act Section 4(a)(6)(C) requires a crowdfunding transaction to be conducted through a broker or funding portal that complies with the requirements of Securities Act Section 4A(a). The term "broker" is generally defined in Exchange Act Section 3(a)(4) as any person that effects transactions in securities for the account of others. Exchange Act Section 3(a)(80) defines the term "funding portal" as any person acting as an intermediary in a transaction involving the offer or sale of securities for the account of others, solely pursuant to Securities Act Section 4(a)(6), that does not: (1) offer investment advice or recommendations; (2) solicit purchases, sales or offers to buy the securities offered or displayed on its website or portal; (3) compensate employees, agents or other persons for such solicitation or based on the sale of securities displayed or referenced on its website or portal; (4) hold, manage, possess or otherwise handle investor funds or securities; or (5) engage in such other activities as the Commission, by rule, determines appropriate.[589]

In the Proposing Release, we explained that because a funding portal would be engaged in the business of effecting securities transactions for the accounts of others through crowdfunding, it

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588 Trust Indenture Act Section 304(a)(8) [15 U.S.C. 77ddd(a)(8)] and Rule 4a-1 [17 CFR 260.4a-1] also provide an exemption to issue up to $5 million of debt securities without an indenture in any 12-month period.

589 Congress in the JOBS Act inadvertently created two Sections 3(a)(80) in the Exchange Act, the other being the definition of "emerging growth company" (added by Section 101(b) of Title I of the JOBS Act).

would be a "broker" within the meaning of Section 3(a)(4) of the Exchange Act.[590] Accordingly, proposed Rule 300(c)(2) of Regulation Crowdfunding would define "funding portal" consistent with the statutory definition of "funding portal," with the substitution of the word "broker" for the word "person."

We also stated in the Proposing Release that the proposed rules would apply not only to funding portals, but also to their associated persons in many instances. The terms "person associated with a broker or dealer" and "associated person of a broker or dealer" are defined in Exchange Act Section 3(a)(18).[591] Proposed Rule 300(c)(1) of Regulation Crowdfunding would similarly define the term "person associated with a funding portal or associated person of a funding portal" to mean any partner, officer, director or manager of a funding portal (or any person occupying a similar status or performing similar functions), any person directly or indirectly controlling or controlled by a funding portal, or any employee of a funding portal, other than persons whose functions are solely clerical or ministerial. The proposed rules would provide, however, that persons who are excluded from the definition of associated person of a funding portal because their functions are solely clerical or ministerial would remain subject to our sanctioning authority under Exchange Act Sections 15(b)(4) and 15(b)(6).[592] This definition is consistent with, and modeled on, the language of Exchange Act Section 3(a)(18).[593]

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590 *See* Proposing Release at 78 FR 66458. *See also* discussion in Section II.D.2.

591 15 U.S.C. 78c(a)(18).

592 Section 15(b)(4) (15 U.S.C. 78*o*(b)(4)) authorizes the Commission to bring administrative proceedings for the imposition of sanctions, up to and including the revocation of a broker's registration, when the broker violates the federal securities laws (and for other misconduct). Section 15(b)(6) (15 U.S.C. 78*o*(b)(6)) provides similar sanctioning authority with respect to persons associated with a broker, including the ability to bar such persons from associating with any Commission registrant.

593 We note, however, that the definition in proposed Rule 300(c)(1) does not include persons under common control with the funding portal, unlike the definition in Exchange Act Section 3(a)(18) which includes such persons as associated persons of broker-dealers.

In proposed Rule 300(c)(4), we also defined "investor" as any investor or any potential investor, as the context requires.

b. Comments on the Proposed Rules

The Proposing Release requested comments on whether there were funding portal activities, other than those in Exchange Act Section 3(a)(80), that we should prohibit, and whether any prohibitions should be modified or removed. We also requested comments about whether further guidance was necessary on the provisions of the Exchange Act and the rules and regulations thereunder that would apply to funding portals.

Some commenters stated that the Commission should not provide any further guidance or prohibitions on funding portal activity in addition to those required by statute.[594] One of these commenters stated that the proposed regulations for funding portal activities are "sufficient for investor protection and proper regulatory oversight."[595] Another commenter opposed removing or modifying the statutory limitations on funding portal activities, stating that if funding portals wish to engage in the prohibited activities, they could do so by registering, and being appropriately regulated as, broker-dealers.[596]

c. Final Rules

After considering the comments, we are adopting, as proposed, the definitions of "associated person of a funding portal or person associated with a funding portal" and "funding

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594 *See, e.g.*, RocketHub Letter; Tiny Cat Letter (stating that the proposed regulations provide a "healthy level of investor protection, but are not overly burdensome and we wholeheartedly appreciate the [C]ommission's general attitude of restraint"). Another commenter also opposed additional prohibitions, stating that "to add prohibitions would be an illegal Rule not authorized by the JOBS Act legislation." *See* Public Startup Letter 2. This commenter made a similar argument with respect to various aspects of the rule. We note, however, that the JOBS Act provides the Commission the authority to provide other requirements for the protection of investors and in the public interest. *See, e.g.*, Securities Act Section 4A(a)(12); 4A(b)(5).

595 *See* Tiny Cat Letter.

596 *See* Consumer Federation Letter.

portal" in Rules 300(c)(1) and(2), respectively. In particular, we believe that, at the present time, the statutory prohibitions on a funding portal in Exchange Act Section 3(a)(80), as reflected in the final rule definition of a funding portal, provide appropriate investor protections.

We also are adopting the definition of "investor" from the proposed rules but have moved the definition to Rule 100(d), and made a modification to clarify that the definition applies to all of Regulation Crowdfunding.[597] Although commenters did not address the definition of "investor," we are making this change to address any potential confusion about whether the definition is applicable to all of Regulation Crowdfunding.

2. General Requirements for Intermediaries

a. Registration and SRO Membership

(1) Proposed Rules

Securities Act Section 4A(a)(1) requires that a person acting as an intermediary in a crowdfunding transaction register with the Commission as a broker or as a funding portal.[598] Proposed Rule 300(a)(1) of Regulation Crowdfunding would implement this requirement by providing that a person acting as an intermediary in a transaction involving the offer or sale of securities made in reliance on Section 4(a)(6) must be registered with the Commission as a broker under Exchange Act Section 15(b), or as a funding portal pursuant to Section 4A(a)(1) and proposed Rule 400 of Regulation Crowdfunding. As discussed below, we also proposed to make the information that a funding portal provides on the proposed registration form (*i.e.*, Form

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597 *See* Section II.B.1.

598 As we noted in the Proposing Release, facilitating crowdfunded transactions (which involve the offer or sale of securities by an issuer and not secondary market activity) alone would not require an intermediary to register as an exchange or as an alternative trading system (*i.e.*, registration as a broker-dealer subject to Regulation ATS). *See* Proposing Release at 78 FR 66459 (discussing secondary market activity and exchange or ATS registration).

Funding Portal), other than personally identifiable information or other information with a significant potential for misuse, accessible to the public.[599]

Securities Act Section 4A(a)(2) requires an intermediary to register with any applicable self-regulatory organization ("SRO"), as defined in Exchange Act Section 3(a)(26).[600] Exchange Act Section 3(h)(1)(B) separately requires, as a condition of the exemption from broker registration, that a funding portal be a member of a national securities association that is registered with the Commission under Exchange Act Section 15A. Proposed Rule 300(a)(2) would implement these provisions by requiring an intermediary in a transaction involving the offer or sale of securities made in reliance on Section 4(a)(6) to be a member of FINRA or any other national securities association registered under Exchange Act Section 15A. Currently, FINRA is the only registered national securities association.

We also proposed definitions for the terms "intermediary" and "SRO" in proposed Rules 300(c)(3) and 300(c)(5) of Regulation Crowdfunding, respectively. As proposed, intermediary would mean a broker registered under Section 15(b) of the Exchange Act or a funding portal registered under proposed Rule 400 of Regulation Crowdfunding and would include, where relevant, an associated person of the registered broker or registered funding portal. SRO was proposed to have the same meaning as in Section 3(a)(26) of the Exchange Act.

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599 *See* Section II.D.1 (discussing registration requirements).

600 15 U.S.C. 78c(a)(26). Exchange Act Section 3(a)(26) defines an "SRO" to include, among other things, a "registered securities association." *Id.*

(2) Comments on the Proposed Rules

Commenters generally supported FINRA being the appropriate SRO and national securities association for intermediaries.[601] In the Proposing Release, we asked if we were to approve the registration of another national securities association under Exchange Act Section 15A in the future, in addition to FINRA, whether it would it be appropriate for us to require membership in both the existing and new association. Commenters urged that intermediaries be required to register with only one such national securities association.[602]

Certain commenters expressed concern about potential competitive advantages of registered broker-dealers over funding portals, suggesting that the Commission should prohibit brokers from engaging in transactions conducted pursuant to Section 4(a)(6) until funding portals can become registered,[603] or provide funding portals a grace period so they may be able to operate before their registration becomes effective.[604] Another commenter, however, suggested that licensed broker-dealers should be immediately authorized to provide services associated with a "registered crowdfunding portal" to any issuer looking to self-host or to an issuer that has "an offline mechanism available for crowdfunding."[605]

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601 *See*, *e.g.*, Joinvestor Letter; RocketHub Letter. One commenter stated that funding portals should not be required to register with the Commission or become FINRA members because, unlike brokers, they serve only as an "information delivery service." *See* Perfect Circle Letter. We note, however, that registration is a statutory requirement under Securities Act Section 4A(a)(1).

602 *See*, *e.g.*, Joinvestor Letter; Public Startup Letter 2; RocketHub Letter; Vann Letter.

603 *See*, *e.g.*, RocketHub Letter.

604 *See*, *e.g.*, Joinvestor Letter.

605 Public Startup Letter 2.

In response to our requests for comment in the Proposing Release, commenters were also divided on whether the Commission should require minimum qualification, testing and licensure requirements for funding portals and their associated persons. [606]

(3) Final Rules

After considering the comments, we are adopting Rule 300(a) generally as proposed but deleting specific references to FINRA in the final rule, as well as the rest of Regulation Crowdfunding and Form Funding Portal, when referring to a registered national securities association. Although we recognize that FINRA is currently the only registered national securities, we believe it is redundant to specifically include its name when referring to registered national securities associations in the rule text and Form Funding Portal.

We are cognizant of the fact that funding portals must register with the Commission and become compliant with an entirely new set of rules. The effective date for the final rules (which is 180 days after publication in the Federal Register, except for § 227.400, Form Funding Portal, and the amendments to Form ID, which are effective January 29, 2016) is designed to provide a sufficient amount of time for funding portals to register and establish the necessary infrastructure to comply with other requirements being imposed in Regulation Crowdfunding before any intermediaries – either broker-dealers or funding portals – may engage in crowdfunding activities. We believe this should address commenters' concerns that broker-dealers otherwise may gain a

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606 Comments in support included Hakanson Letter; Reichman Letter; RocketHub Letter. *See also* CrowdCorp Letter (stating that the Commission should establish a separate licensing scheme for persons who help prepare issuer disclosure documents and advise issuers, but who are not brokers or funding portals). Comments opposed included Public Startup Letter 2; Startup Valley Letter.

competitive advantage if they were able to engage in crowdfunding activities before funding portals are able to comply with the requirements needed to begin operation.[607]

While FINRA is the only registered national securities association at present, we recognize that a new national securities association or associations could register with us in the future. At that time, a funding portal could choose to become a member of the new association(s) instead of, or in addition to, its FINRA membership. As we noted above, we requested comment on whether we should require membership in both the existing national securities association (FINRA) and a new national securities association, if we were to approve another national securities association in the future. We have considered commenters' views and have determined not to require that funding portals be members of multiple securities associations (should new associations be registered in the future). Because all registered national securities associations must satisfy the same statutory standards set forth in Exchange Act Section 15A, we do not believe at this time that requiring membership in additional associations would add significant investor protections.

After considering comments, we have determined not to impose any licensing, testing or qualification requirements for associated persons of funding portals. We believe that a registered national securities association is well-positioned, given the requirements for registration as a national securities association, as well as the statutory and regulatory requirements that apply to

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607 We note that broker-dealers may nonetheless have a competitive advantage to the extent that they are able to provide a wider range of services than those permitted funding portals under the statute. However, we believe this competitive advantage is balanced to a significant degree by a strong regulatory regime tailored to that wider range of services.

such a registered entity, to determine whether to propose additional requirements such as licensing, testing or qualification requirements for associated persons of funding portals.[608]

We also are adopting as proposed the definitions for the terms "intermediary" in Rule 300(c)(3). However, we are removing the definition of "self-regulatory organization" and "SRO" from the final rules because the term is already defined in Exchange Act Section 3(a)(26).

b. Financial Interests

(1) Proposed Rules

Securities Act Section 4A(a)(11) requires an intermediary to prohibit its directors, officers or partners (or any person occupying a similar status or performing a similar function) from having any financial interest in an issuer using its services. In the Proposing Release, we proposed to use our discretion to extend the prohibition to the intermediary itself. Thus, proposed Rule 300(b) of Regulation Crowdfunding would prohibit the intermediary, as well as its directors, officers or partners (or any person occupying a similar status or performing a similar function), from having: (1) a financial interest in an issuer using its services; and (2) from receiving a financial interest in the issuer as compensation for services provided to, or for the benefit of, the issuer, in connection with the offer and sale of its securities. Proposed Rule 300(b) defined "a financial interest in an issuer" to mean a direct or indirect ownership of, or economic interest in, any class of the issuer's securities.

608 All SROs are required to file proposed rules and rule changes with us under Exchange Act Section 19(b) and Rule 19b–4. In general, the Commission reviews proposed SRO rules and rule changes and publishes them for comment. The Commission then approves or disapproves them, or the rules become effective immediately or by operation of law.

(2) Comments on the Proposed Rules

In general, commenters supported the Commission's proposed financial interest prohibition as it applies to an intermediary's directors, officers or partners (or any person occupying a similar status or performing a similar function),[609] as well as the proposed definition of financial interest.[610] In contrast, however, many commenters opposed the Commission's proposed prohibition on an intermediary itself having or receiving a financial interest in the issuer,[611] while some supported this proposed prohibition.[612]

Commenters who supported our proposal to extend the prohibition on financial interests to the intermediary suggested that such prohibitions may help to mitigate conflicts of interests.[613] One commenter stated that an intermediary having a financial interest in the issuer would skew the incentives of the intermediary toward its own interests rather than the integrity of the transaction, and also stated its view that disclosure of this interest could not cure this problem.[614]

Several commenters who opposed the prohibition on an intermediary having a financial interest in the issuer suggested that the prohibition would reduce the number and types of

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609 *See, e.g.*, CFA Institute Letter; Consumer Federation Letter; Jacobson Letter.

610 *See, e.g.*, Hackers/Founders Letter; Joinvestor Letter; Tiny Cat Letter. *See also* Consumer Federation Letter (stating that the Commission should "monitor practices in this area once rules are adopted to ensure that the intended limits appropriate to intermediaries' gatekeeper functions are not being circumvented through the use of other types of payments or financial arrangements").

611 *See, e.g.*, AngelList Letter; Anonymous Letter 3; Arctic Island Letter 6; EMKF Letter; Growthfountain Letter; Guzik Letter 1; Hackers/Founders Letter; Heritage Letter; Milken Institute Letter; Propellr Letter 1; Public Startup Letter 2; RoC Letter; RocketHub Letter; Seyfarth Letter; Thomas Letter 1.

612 *See, e.g.*, CFA Institute Letter; Clapman Letter; Consumer Federation Letter; Jacobson Letter; Joinvestor Letter.

613 *See, e.g.*, CFA Institute Letter; Consumer Federation Letter ("An intermediary that is compensated through receipt of a financial interest in an issuer may have an incentive to take steps to ensure that the issuer reaches its funding target so that the offering can move forward or engage in other practices designed to artificially inflate the value of its securities."); Jacobson Letter.

614 *See* Jacobson Letter.

intermediaries that might otherwise participate in crowdfunding activities.[615] These commenters asserted that allowing an intermediary to take this financial interest would provide an option through which issuers could provide payment to the intermediary for its services, and also permit co-investments, which would ultimately benefit investors.[616] These commenters also asserted that such a financial interest could align the interests of intermediaries with those of investors.[617] One commenter suggested that "by removing an upfront cost and incentivizing an ongoing relationship between the intermediary and the issuer, equity compensation for intermediaries fulfils the Commission's twin aims of efficient capital markets and investor protection."[618] Another commenter noted that permitting the intermediary to take a financial interest in the issuer would encourage the development of funding portals that are sponsored by or affiliated with Community Development Financial Institutions ("CDFIs").[619] Yet another commenter suggested that

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615 *See, e.g.*, Hackers/Founders Letter ("Furthermore, rules that preclude the [i]ntermediary from holding any financial interest would overly restrict the [i]ntermediary environment; for example, such restrictions might prevent a diverse set of platforms from developing that serve the specific needs of different communities. The impact of which might disproportionately impact certain communities, such as the not-for-profit community.").

616 *See, e.g.*, EMKF Letter ("The current proposed rules with a fee-based system is a recipe for disaster. No credible startups that have viable alternatives would choose to pay 5-15% of their fundraising round in cash to an intermediary.").

617 *See, e.g.*, AngelList Letter ("So long as the program was consistently applied without judgment by the intermediary, the net effect would purely be to align the interests of the intermediary with the investor."). *See also* EMKF Letter; Hackers/Founders Letter; Heritage Letter; Milken Institute Letter; RoC Letter; Thomas Letter 1.

618 Seyfarth Letter.

619 *See* Concerned Capital Letter (suggesting the Commission broaden the definition of intermediaries to encourage portals sponsored by and/or affiliated with U.S. Treasury-recognized CDFIs and exempt such portals from the prohibitions against having a financial interest in issuers). *See also* City First Letter (suggesting that the Commission allow CDFIs to act as co-lenders).

The Community Development Financial Institutions Fund, which was established by the Riegle Community Development and Regulatory Improvement Act of 1994, is a government program that promoted access to capital and local economic growth by, among other things, investing in, supporting and training CDFIs that provide loans, investments, financial services and technical assistance to underserved populations and communities. *See generally* http://www.cdfifund.gov/what_we_do/programs_id.asp?programID=9. A certified Community Development Financial Institution ("CDFI") is a specialized financial institution that works in market niches that are underserved by traditional financial institutions. CDFIs provide a unique

permitting the intermediary to take a financial interest in the issuer would incentivize intermediaries to screen potential issuers for possible fraud or wrongdoing.[620] Other commenters supported permitting the intermediary to take a financial interest in the issuer so long as the terms of the financial interests taken by the intermediary are the same as or not more favorable than those taken by investors in the offering.[621] Commenters suggested additional measures, such as adequate disclosure,[622] a five percent interest limitation,[623] and restrictions on the ability of an intermediary to transfer its interests in the issuer, could help to address any conflicts of interest concerns.[624]

(3) Final Rules

After considering the comments, we are adopting Rule 300(b), as proposed, with respect to an intermediary's directors, officers or partners (or any person occupying a similar status or performing a similar function). Rule 300(b), as adopted, prohibits an intermediary's directors, officers or partners (or any person occupying a similar status or performing a similar function) from having any financial interest in an issuer using its services. Rule 300(b) also specifically prohibits these persons from receiving a financial interest in the issuer as compensation for services provided to, or for the benefit of, the issuer, in connection with the offer and sale of its

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range of financial products and services in economically distressed target markets, such as mortgage financing for low-income and first-time homebuyers and not-for-profit developers, flexible underwriting and risk capital for needed community facilities, and technical assistance, commercial loans and investments to small start-up or expanding businesses in low-income areas. CDFIs include regulated institutions such as community development banks and credit unions, and non-regulated institutions such as loan and venture capital funds.

620 *See* Anonymous Letter 3.

621 *See, e.g.*, Hackers/Founders Letter; Propellr 1 Letter; Public Startup Letter 2; RocketHub Letter.

622 *See, e.g.*, Growthfountain Letter; Hackers/Founders Letter; Propellr Letter 1; RoC Letter; RocketHub Letter.

623 *See* RocketHub Letter.

624 *See* Hackers/Founders Letter.

securities. Consistent with the proposal, Rule 300(b), as adopted, defines "a financial interest in an issuer" to mean a direct or indirect ownership of, or economic interest in, any class of the issuer's securities. [625]

We are not adopting, however, the proposed complete prohibition on the intermediary itself having or receiving a financial interest in an issuer using its services. Although intermediaries are generally prohibited under the rule as adopted from having such a financial interest, as discussed below, in response to comments, we have amended the rule to permit an intermediary to have a financial interest in an issuer that is offering or selling securities in reliance on Section 4(a)(6) through the intermediary's platform, provided that: (1) the intermediary receives the financial interest from the issuer as compensation for the services provided to, or for the benefit of, the issuer in connection with the offer or sale of such securities being offered or sold in reliance on Section 4(a)(6) through the intermediary's platform; and (2) the financial interest consists of securities of the same class and having the same terms, conditions and rights as the securities being offered or sold in reliance on Section 4(a)(6) through the intermediary's platform.

We are mindful of concerns raised by commenters that a prohibition could have a chilling effect on the ability of small issuers to use the crowdfunding exemption. These issuers may be small businesses or neighborhood establishments that may not have the liquid capital to

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625 As we explained in the Proposing Release, the prohibition is intended to protect investors from the conflicts of interest that may arise when the persons facilitating a crowdfunding transaction have a financial stake in the outcome. 78 FR at 66461. The prohibition extends to "any person occupying a similar status or performing a similar function," and applies with respect to both direct or indirect ownership of, or economic interest in, any class of the issuer's securities. In addition, we note that Section 15(b) of the Securities Act creates liability for persons who aid and abet violations of the Securities Act or the rules and regulations thereunder, such as would occur if a third person knowingly or recklessly provided substantial assistance to a director, officer or partner (or any person occupying a similar status or position), for example, by accepting and holding, on the officer's behalf, a financial interest in the issuer in circumvention of the prohibition.

compensate intermediaries for services. As commenters noted, allowing an intermediary to have or receive a financial interest in the issuer could provide a method for the issuer to pay an intermediary for its services, which may facilitate capital formation. This may, in turn, encourage the development of funding portals that are, for example, affiliated with CDFIs, as one commenter suggested.[626] As commenters further noted, permitting such a financial interest may also help to align the interests of intermediaries and investors, and provide an additional incentive to screen for fraud. We believe at this time the interest of promoting capital formation for small businesses, and developing a workable framework for securities-based crowdfunding, counsels against extending the prohibition on financial interests to the intermediary itself.

However, we are cognizant of the potential conflicts of interest that may arise, and therefore we are placing certain conditions on the ability of intermediaries to have a financial interest in an issuer that is offering or selling securities in reliance on Section 4(a)(6) through the intermediary's platform.[627] First, the intermediary must receive the financial interest from the issuer as compensation for the services provided to, or for the benefit of, the issuer in connection with the offer or sale of such securities being offered or sold in reliance on Section 4(a)(6).[628] We believe that this limitation, which will allow intermediaries to receive securities as payment for services but not otherwise permit them to invest in the offering, addresses commenters' concerns

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[626] *See* Concerned Capital Letter.

[627] *See* notes 613-614 and accompanying text.

[628] As noted above in Section II.C.2, an intermediary must be either a registered funding portal or a registered broker-dealer, and must be a member of a registered national securities association. FINRA rules currently require that its broker-dealer members charge reasonable fees for their services and observe just and equitable principles of trade in the conduct of their business. FINRA has also filed a proposed rule change with the Commission to apply certain rules to funding portals, including requiring them to observe high standards of commercial honor and just and equitable principles of trade in the conduct of their businesses. *See* Proposed Rule Change to Adopt the Funding Portal Rules and Related Forms and FINRA Rule 4518, SR-FINRA-2015-040 (Oct. 9, 2015).

that a prohibition could have a "chilling effect" on the ability of small issuers to use the crowdfunding exemption, while serving to mitigate concerns relating to intermediaries taking steps to "artificially inflate" the value of securities in the offerings.[629] Second, we have considered the comments in support of limiting an intermediary's financial interest by requiring that such interest be the same as or not more favorable than those taken by investors in the offering,[630] and have determined to prohibit intermediaries from receiving a financial interest unless it is in securities that are of the same class, and that have the same terms, conditions and rights as the securities in the offering. We believe that this limitation will further serve to mitigate any potential conflicts by helping to align the interests of the intermediary with those of the investors in the offering.[631]

We are persuaded that the disclosures otherwise required by Regulation Crowdfunding also will help to address any potential conflicts of interest arising from an intermediary having or receiving a financial interest in an issuer. Among other things, Rule 302(d) requires an intermediary to clearly disclose the manner in which it will be compensated in connection with offerings and sales of securities made in reliance on Section 4(a)(6) at account opening and Rule 303(f) requires disclosure of remuneration received by an intermediary (including securities received as remuneration) on confirmations.[632] We believe that these disclosures will provide

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629 *See* Consumer Federation Letter.

630 *See* note 621.

631 The rule does not preclude an intermediary from receiving securities as compensation for services from the same issuer for a subsequent offering conducted by the issuer in reliance on Section 4(a)(6) as long as the securities received are compensation for services provided during the subsequent offering and are of the same class and have the same terms, conditions and rights as the securities being offered in the subsequent offering.

632 *See* Sections II.C.4.d and II.C.5.f. *See also* Rule 302(c) of Regulation Crowdfunding (requiring intermediaries to inform investors, at the time of account opening, that promoters must clearly disclose in all

investors with relevant information concerning any intermediary's financial interests (including whether such interest was acquired on the same terms that are available to investors), which, in turn, will help investors to make better informed investment decisions. In addition, the intermediary must comply with all other applicable requirements of Regulation Crowdfunding, including the statutory limitations on a funding portal's activities.[633]

Commission staff expects to review the compensation structure of intermediaries during the study of the federal crowdfunding exemption it plans to undertake no later than three years following the effective date of Regulation Crowdfunding.[634]

3. Measures to Reduce Risk of Fraud

Securities Act Section 4A(a)(5) requires an intermediary to "take such measures to reduce the risk of fraud with respect to [transactions made in reliance on Section 4(a)(6)], as established by the Commission, by rule, including obtaining a background and securities enforcement regulatory history check on each officer, director, and person holding more than 20 percent of the outstanding equity of every issuer whose securities are offered by such person." As discussed

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communications on the platform the receipt of compensation and the fact that he or she is engaging in promotional activities on behalf of the issuer).

633 *See* Exchange Act Section 3(a)(80) (defining "funding portal" and establishing certain limitations on their activities consistent with the statute, such as prohibiting a funding portal from offering investment advice or recommendation; soliciting purchases, sales or offers to buy securities offered or displayed on its website or portal; or holding, managing, possessing, or otherwise handling investor funds or securities). In this regard, compliance with disclosures required by Regulation Crowdfunding generally would not cause a funding portal to provide investment advice or recommendations. Nonetheless, a funding portal should seek to ensure that disclosure of its financial interest(s) in an issuer is not inconsistent with the statutory prohibition on providing investment advice or recommendations. For example, a funding portal must not present its financial interest in an issuer as a recommendation or endorsement of that issuer. *See* Section II.D.3. We also note that if a funding portal holds, owns or proposes to acquire securities issued by an issuer, or multiple issuers, that individually or in aggregate exceed more than 40% of the value of the funding portal's total assets (excluding government securities and cash items) on an unconsolidated basis, the funding portal may fall within the definition of investment company under Section 3(a)(1)(C) of the Investment Company Act. We generally would expect, however, that such funding portal would seek to rely on the exclusion from the definition of investment company in Section 3(c)(2) of the Investment Company Act for (among other things) a person primarily engaged in the business of acting as a broker.

634 *See* Section II.

below, after considering the comments, we are adopting Rule 301 of Regulation Crowdfunding substantially as proposed, with a few changes to Rule 301(c)(2).

a. Issuer compliance

(1) Proposed Rule

We proposed in Rule 301(a) of Regulation Crowdfunding to require that an intermediary have a reasonable basis for believing that an issuer seeking to offer or sell securities though the intermediary's platform complies with the requirements of Section 4(a)(6) and the related requirements of Regulation Crowdfunding. For this requirement, we proposed that an intermediary may reasonably rely on an issuer's representations about compliance unless the intermediary has reason to question the reliability of those representations.

(2) Comments on Proposed Rule

Commenters generally agreed that intermediaries play a significant role in preventing and detecting fraud and should take measures to reduce potential fraud. Some commenters, however, expressed concerns about the proposed "reasonable basis" standard for an intermediary's belief about an issuer's compliance with applicable laws stating that the standard should be higher.[635] Others commenters supported the standard.[636]

A number of commenters expressed concern about the proposed reliance on issuer representations.[637] Some commenters suggested an intermediary should be required to conduct

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635 *See*, *e.g.*, AFR Letter; ASTTC Letter; Computershare Letter; Consumer Federation Letter; CSTTC Letter; Grassi Letter; Merkley Letter; NYSSCPA Letter.

636 *See*, *e.g.*, RocketHub Letter; STA Letter.

637 *See*, *e.g.*, AFR Letter; Computershare Letter; Consumer Federation Letter; Merkley Letter.

some type of due diligence on the issuer, as opposed to relying on issuer representations.[638] Another commenter went further by suggesting that an intermediary should also have an ongoing obligation to monitor communications by issuers during the course of the offering to detect and prevent violations of the securities laws and the regulations thereunder.[639] Another commenter stated that an issuer's representation should not suffice unless it is detailed enough to evidence a reasonable awareness by the issuer of its key obligations and the ability to comply with those obligations.[640]

One commenter argued that the language of the proposed rule was contradictory because relying on representations made by the issuer is not the same as establishing a reasonable basis for believing the issuer is in compliance.[641]

One commenter recommended that the Commission "consider a tiered approach to compliance obligations" where, as the size of the offering or other risk factors increased, intermediaries would be required to conduct more rigorous compliance reviews.[642] Under such an approach, this commenter stated that for small offerings that cap investments at a low level, $500 for example, and where there is no participation by individuals with a history of security law violations, the intermediary would be permitted to rely on representations by issuers to satisfy its

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638 *See*, *e.g.*, CSTTC Letter; Grassi Letter; NYSSCPA Letter; Consumer Federation Letter (stating that an intermediary's responsibility is rendered meaningless without establishing specific standards that require due diligence in order to reasonably conclude the issuer is in compliance).

639 *See* AFR Letter ("[T]he Commission's proposal to allow intermediaries to rely on self-certification by issuers makes a mockery of its proposed requirement that intermediaries have 'a reasonable basis for believing that an issuer seeking to offer and sell securities in reliance on Section 4(a)(6), through the intermediary's platform, complies with the requirements in Securities Act Section 4A(b) and the related requirements in Regulation Crowdfunding.'").

640 *See* STA Letter.

641 *See* ABA Letter.

642 *See* IAC Recommendation; *see also* BetterInvesting Letter.

obligation to ensure compliance. As the size of the offering, the size of permitted investments, or other risk factors increase, the commenter stated that the Commission should consider requiring intermediaries to conduct more rigorous compliance reviews.

(3) Final Rule

Rule 301(a), as adopted, requires that an intermediary have a reasonable basis for believing that an issuer seeking to offer and sell securities in reliance on Section 4(a)(6) through the intermediary's platform complies with the requirements in Securities Act Section 4A(b) and the related requirements in Regulation Crowdfunding. While some commenters argued for higher or different standards, such as requiring intermediaries to conduct due diligence on issuers or monitor communications by issuers during the course of the offering, we believe that a reasonable basis standard is appropriate, particularly in view of the issuer's own obligation to comply with the requirements in Section 4A(b) and the related requirements in Regulation Crowdfunding. We are mindful as well of the associated costs of a potentially higher standard. Consistent with the proposal, Rule 301(a) also permits intermediaries to reasonably rely on representations of the issuer, unless the intermediary has reason to question the reliability of those representations.

In satisfying the requirements of Rule 301(a), we emphasize that an intermediary has a responsibility to assess whether it may reasonably rely on an issuer's representation of compliance through the course of its interactions with potential issuers.[643] We agree with comments that an intermediary seeking to rely on an issuer representation should consider whether the

[643] In addition, an intermediary's potential liability under Securities Act Section 4A(c), as added by the JOBS Act, may encourage intermediaries to develop adequate procedures to fully assess whether reliance on an issuer's representation is reasonable. We also note that Congress provided a defense to any such liability if an intermediary did not know, and in the exercise of reasonable care could not have known, of the untruth or omission. Therefore, and as identified in the Proposing Release, we continue to believe that there are appropriate steps that intermediaries might take in exercising reasonable care in light of this liability provision. *See* Section II.E.5 (discussing scope of statutory liability).

representation is detailed enough to evidence a reasonable awareness by the issuer of its obligations and its ability to comply with those obligations. The specific steps an intermediary should take to determine whether it can rely on an issuer representation may vary, but should be influenced by and tailored according to the intermediary's knowledge and comfort with each particular issuer. We believe this approach is generally consistent with the view of one commenter that suggested a tiered approach to compliance obligations where intermediaries should conduct more rigorous compliance reviews and background checks as risk factors increase.[644]

b. Records of Securities Holders

(1) Proposed Rule

We proposed in Rule 301(b) of Regulation Crowdfunding a requirement that an intermediary have a reasonable basis for believing that an issuer has established means to keep accurate records of the holders of the securities it would offer and sell through the intermediary's platform. We proposed that an intermediary may reasonably rely on an issuer's representations about compliance unless the intermediary has reason to question the reliability of those representations. We did not propose a particular form or method of recordkeeping of securities, nor did we propose to require that an issuer use a transfer agent or other third party.[645] We noted, however, that requiring a registered transfer agent to be involved after the offering could introduce a regulated entity with experience in maintaining accurate shareholder records,[646] and we asked in

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644 We also emphasize that when an intermediary seeks to rely on the representations of others to form a reasonable basis, the intermediary should have policies and procedures regarding under what circumstances it can reasonably rely on such representations and when additional investigative steps may be appropriate. *See* Section II.D.4.

645 Proposing Release, 78 FR at 66462

646 *Id.*

the Proposing Release whether we should require an issuer to use a regulated transfer agent to keep such records and whether there were less costly means by which an issuer could rely on a third party to assist with the recordkeeping.[647]

(2) Comments on Proposed Rule

Commenters agreed that an intermediary should have a basis for believing that an issuer has established a means to keep accurate records.[648] Commenters were divided, however, between those who supported[649] and those who opposed[650] any requirement mandating the use of a registered transfer agent. Commenters supporting the required use of registered transfer agents cited potential benefits, including reducing internal costs and providing corporate transparency;[651] having the transfer agent serve as the issuer's paying agent, proxy agent, exchange agent, tender agent and mailing agent for ongoing reports;[652] providing a back-up and recovery system for records;[653] and conducting internal audits to protect against theft.[654] Some commenters also highlighted potential problems when non-registered transfer agents or the issuer maintains records, including improper registration of multiple owners, duplicate records, missing certificate

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647 *Id.* at 66464.

648 *See*, *e.g.*, Arctic Island Letter 5; ASTTC Letter; CFIRA Letter 8; Computershare Letter; CST Letter; CSTTC Letter; FAST Letter; Grassi Letter; Joinvestor Letter; Public Startup Letter 2; RocketHub Letter; STA Letter; Tiny Cat Letter.

649 *See*, *e.g.*, ASTTC Letter; ClearTrust Letter; CST Letter; CSTTC Letter; Empire Stock Letter; Equity Stock Letter; FAST Letter; Sharewave Letter; Stalt Letter.

650 *See*, *e.g.*, Arctic Island Letter 5; CapSchedule Letter; CFIRA Letter 8; Computershare Letter; Grassi Letter; Joinvestor Letter; NYSSCPA Letter; Public Startup Letter 2; RocketHub Letter; Tiny Cat Letter.

651 *See* CST Letter.

652 *See* Empire Stock Letter.

653 *See* FAST Letter.

654 *Id.*

numbers, inability to trace ownership, and inability to maintain records;[655] and incorrect handling of corporate actions, failure to observe restrictions on transfers, and failure to follow abandoned property reporting requirements.[656] One commenter suggested that the Commission should identify specific areas for an intermediary to consider about an issuer's recordkeeping capabilities when determining whether or not to provide access to that issuer.[657] This commenter also urged the Commission to create a safe harbor whereby an intermediary would be deemed to have met the recordkeeping requirement if the issuer has retained a registered transfer agent or registered broker-dealer.[658]

Commenters that opposed the mandatory use of a registered transfer agent pointed to cost concerns.[659] Some of these commenters stated that alternatives to transfer agents will develop, including CPA firms,[660] registered broker-dealers[661] and software applications or other potential low-cost alternatives.[662] Some commenters stated that intermediaries should be permitted to provide the relevant recording services to issuers.[663] One commenter suggested funding portals

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655 *See, e.g.*, ClearTrust Letter; STA Letter; Stalt Letter.

656 *See* STA Letter.

657 *Id.*

658 *Id.* The commenter also stated that such a safe harbor would encourage third-party recordkeepers to register as transfer agents and thereby enhance protection to investors. The commenter further stated that the safe harbor should not apply if a community bank is utilized because it would not have similar recordkeeping experience. *See also* Computershare Letter (stating that a safe harbor should apply if another regulated entity, such as a broker-dealer or a bank, is engaged to perform the services, which in turn may encourage the use of professional regulated recordkeepers, thus enhancing overall protection in the crowdfunding market).

659 *See, e.g.*, AICPA Letter; Arctic Island Letter 5; CapSchedule Letter; CFIRA Letter 8; Computershare Letter; Grassi Letter; Joinvestor Letter; RocketHub Letter; STA Letter; Tiny Cat Letter.

660 *See, e.g.*, Grassi Letter; NYSSCPA Letter.

661 *See* Public Startup Letter 2.

662 *See* Arctic Island Letter 5.

663 *See, e.g.*, Joinvestor Letter; RocketHub Letter.

should only be permitted to do so with respect to securities purchased on their platform or transferred among platforms, such that they would not be permitted to act as "full-fledged [b]rokerage firms or transfer agents."[664]

(3) Final Rules

After considering the comments, we are adopting Rule 301(b), as proposed, with one modification. Rule 301(b) as adopted requires an intermediary to have a reasonable basis for believing that an issuer has established means to keep accurate records of the holders of the securities it would offer and sell through the intermediary's platform, and provides that in satisfying this requirement, an intermediary may rely on the representations of the issuer concerning its means of recordkeeping unless the intermediary has reason to question the reliability of those representations. We also are adding a provision to Rule 301(b) as adopted stating that an intermediary will be deemed to have satisfied this requirement if the issuer has engaged the services of a transfer agent that is registered under Section 17A of the Exchange Act.[665] As we noted in the Proposing Release, we believe that the recordkeeping function may be provided by the issuer, a broker, a transfer agent or some other (registered or unregistered) person. We recognize that, as a commenter explained, recordkeeping functions can be extensive and could include, for example, the ability to (1) monitor the issuance of the securities the issuer offers and sells through the intermediary's platform, (2) maintain a master security holder list reflecting the owners of those securities, (3) maintain a transfer journal or other such log recording any transfer of ownership, (4) effect the exchange or conversion of any applicable securities, (5) maintain a control book demonstrating the historical registration of those securities, and (6) countersign or

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664 *See* RocketHub Letter.

665 15 U.S.C. 78q-1(c). We also note that an issuer's exemption from Section 12(g) is conditioned on, among other things, that issuer engaging a registered transfer agent. *See* Section II.E.4.

legend physical certificates of those securities. While the use of a registered transfer agent could introduce a regulated entity with experience in maintaining accurate shareholder records, as noted in the Proposing Release, we believe the issuer should have flexibility in establishing such means, and that such flexibility may allow for competition among service providers that could reduce operating costs for funding portals. We continue to believe that accurate recordkeeping can be accomplished by diligent issuers or through a variety of third parties. We note also that, for investors to have confidence in crowdfunding, issuers and intermediaries must have a shared interest in ensuring stability and accuracy of records. Therefore, intermediaries should consider the numerous obligations required of a record holder when determining whether an issuer has established a reasonable means to keep accurate records of the security holders being offered and sold securities through the intermediary's platform.

At the same time, mindful of the role that may be played by registered transfer agents in maintaining accurate shareholder records, we are providing a safe harbor for compliance with Rule 301(b) for those issuers that use a registered transfer agent. While we do not intend to provide regulated entities with a competitive advantage over other recordkeeping options that comply with the rule's requirements, we believe it is appropriate to provide certainty as to Rule 301(b) compliance in instances in which an issuer has engaged the services of a transfer agent that is registered under Section 17A of the Exchange Act.

c. Denial of Platform Access

(1) Proposed Rule

We also proposed in Rule 301(c)(1) of Regulation Crowdfunding a requirement that an intermediary deny access by an issuer to its platform if it has a reasonable basis for believing that an issuer, or any of its officers, directors or any person occupying a similar status or performing a

similar function, or any 20 Percent Beneficial Owner is subject to a disqualification under proposed Rule 503.[666] In satisfying this requirement, we proposed to require an intermediary to, at a minimum, conduct a background and securities enforcement regulatory history check on each issuer whose securities are to be offered by the intermediary and on each officer, director or 20 Percent Beneficial Owner.

We further proposed in Rule 301(c)(2) to require an intermediary to deny access to its platform if the intermediary believes the issuer or offering presents the potential for fraud or otherwise raises concerns about investor protection. In satisfying this requirement, the proposed rule would require that an intermediary deny access if it believes that it is unable to adequately or effectively assess the risk of fraud of the issuer or its potential offering. In addition, we proposed in Rule 301(c)(2) that if an intermediary becomes aware of information after it has granted access that causes it to believe the issuer or the offering presents the potential for fraud or otherwise raises concerns about investor protection, the intermediary would be required to promptly remove the offering from its platform, cancel the offering, and return (or, for funding portals, direct the return of) any funds that have been committed by investors in the offering.

(2) Comments on Proposed Rule

Commenters generally supported proposed Rule 301(c).[667] Commenters noted with approval the discretion the proposed rules would provide intermediaries.[668] The "reasonable basis" standard in proposed Rule 301(c)(1) also garnered comments. One commenter suggested

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666 *See* Section II.E.6 (discussing Rule 503 of Regulation Crowdfunding, which describes disqualification).

667 *See, e.g.*, CFA Institute Letter; StartupValley Letter.

668 *Id*.

that the reasonable basis standard was not strong enough.[669] One commenter stated that having a reasonable basis standard in the disqualification determination would be "difficult to imagine" unless the Commission maintains a database for intermediaries to search.[670]

Commenters had varied views on the proposed requirement in Rule 301(c)(1) for an intermediary to perform a background check on the issuer and certain of its affiliated persons. Several commenters supported the requirement, but a few commenters suggested ways to decrease costs.[671] One commenter stated that only low-cost, minimum requirements should be implemented,[672] while another commenter suggested that the background checks be required only after an issuer has met its target offering amount so as to prevent unnecessary expense to the intermediary.[673] Representing a different view, one commenter opposed a requirement for background checks to be conducted on all persons related to an issuer.[674] Another commenter noted that the checks would be appropriate, but did not support the requirement.[675]

Commenters were divided as to whether we should set specific requirements for background checks. One commenter stated that the proposal "fails to set even the most general of standards for these checks" and "instead relies on intermediaries to use their experience and judgment to reduce the risk of fraud."[676] The same commenter stated that the proposed approach

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669 *See* NYSSCPA Letter (opposing the use of two different standards within Rule 301(c) as it could lead to confusion and presents vulnerability for fraud to occur through the "weakest link," and suggesting instead that a "prudent care" standard should be used for both requirements).

670 *See* Public Startup Letter 2.

671 *See*, *e.g.*, AFR Letter; CFA Institute Letter; Grassi Letter; Joinvestor Letter; NYSSCPA Letter**.**

672 *See* RocketHub Letter.

673 *See* Anonymous Letter 4.

674 *See* Zhang Letter.

675 *See* Public Startup Letter 2.

676 *See* Consumer Federation Letter.

is flawed and as such the checks are likely to be ineffective, especially because many intermediaries are likely to be inexperienced.[677] Several commenters requested further clarification and specification about required checks.[678] However, other commenters stated that the Commission should not specify steps for an intermediary to take in conducting checks.[679]

With respect to our request for comment on whether intermediaries should be required to make the results of background checks public, several commenters opposed the requirement,[680] while some supported it.[681] Another commenter stated its view that the results should not be made public unless a regulator called them into question.[682] Another commenter explained that issuers should be able to publish the results if they choose, but no such requirement should be placed on intermediaries.[683] One commenter urged us to "require that a summary of the sources consulted as part of the background check be posted on the [portal's] website."[684]

As to proposed Rule 301(c)(2) requiring a funding portal to deny access if the intermediary believes the issuer or offering presents the potential for fraud or otherwise raises concerns

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677 *Id*.

678 *See*, *e.g.*, BetterInvesting Letter; Heritage Letter; IAC Recommendation; Jacobson Letter; NSBA Letter. *See also* RocketHub Letter (stating that intermediaries "should be allowed to satisfy their obligations by checking commonly used databases for criminal background, bankruptcy filings, and tax liens, as well as cross check against the Office of Foreign Assets Control (OFAC) sanctions lists, and Specially Designated Nationals (SDN) and Blocked Persons lists"); Bullock Letter (recommending fingerprinting for key issuer personnel and noting that most sheriff's departments in most U.S. counties can take fingerprints for a small fee).

679 *See*, *e.g.*, StartupValley Letter; Vann Letter.

680 *See*, *e.g.*, Grassi Letter; Joinvestor Letter; NYSSCPA Letter; Public Startup Letter 2; StartupValley Letter.

681 *See*, *e.g.*, AFR Letter; Consumer Federation Letter.

682 *See* Joinvestor Letter.

683 *See* Public Startup Letter 2.

684 IAC Recommendation (suggesting that "[r]equiring posting of information about the sources consulted in compiling the reports would better enable investors to evaluate the thoroughness of the background check, thus creating an incentive for intermediaries to conduct thorough reviews in the absence of clear Commission guidelines"); *see also* BetterInvesting Letter.

regarding investor protection, one commenter stated that the proposed requirement conflicts with the restrictions on a funding portal's ability to limit the offerings on its platform in proposed Rule 402(b)(1).[685]

Regarding the standard for denial based on potential fraud or investor protection concerns in the proposed rule, one commenter suggested a stronger standard,[686] while another suggested a weaker standard.[687] Other commenters suggested that the standard for an intermediary to deny access to its platform is unclear.[688] One commenter urged the Commission to require that a funding portal post on its website a description of its standards for determining which offerings present a risk of fraud."[689]

One commenter stated the intermediaries should be required to report denied issuers, noting that it would not only help prevent fraud but also assist other intermediaries in excluding issuers already discovered to be disqualified.[690] Other commenters disagreed with this suggestion,[691] while one commenter stated that reporting should be required only if the

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685 *See* Guzik Letter 1 (noting that under the proposed rules, an intermediary which is not a broker-dealer is prohibited from, at least in that commenter's view, "curating," that is, "excluding companies from its platform based upon qualitative factors, such as quality of management, valuation of the company, market size, need for additional capital, pending litigation, or other qualitative factors which increase the risk to an investor").

686 *See* note 669 (discussing the NYSSCPA Letter, which suggested a "prudent care" standard for denying issuers under Rule 301(c)).

687 *See* Grassi Letter (stating that an intermediary "should not be required to vet issuers for potential fraud other than would be done through the normal course of assessing whether they wish to do business with a particular issuer").

688 *See*, *e.g.*, BetterInvesting Letter; Heritage Letter; IAC Recommendation; Jacobson Letter; NSBA Letter.

689 *See* IAC Recommendation; *see also* BetterInvesting Letter.

690 *See* Joinvestor Letter. *See also* ASSOB Letter and Vann Letter.

691 *See*, *e.g.*, Public Startup Letter 2 (opposing the requirement but suggesting that the Commission maintain a database of known bad actors).

Commission or another agency created a database for such information.[692] One of these commenters suggested that intermediaries should be required to notify a potential issuer when the intermediary uses information from a third party to deny the issuer.[693]

(3) Final Rules

After considering the comments, we are adopting Rule 301(c)(1) as proposed. Rule 301(c)(1) requires an intermediary to deny access to its platform if the intermediary has a reasonable basis for believing that an issuer, or any of its officers, directors (or any person occupying a similar status or performing a similar function), or any 20 Percent Beneficial Owner is subject to a disqualification under Rule 503 of Regulation Crowdfunding. We believe that a "reasonable basis" standard for denying access is an appropriate standard for Rule 301(c)(1), in part because this requirement on an intermediary is buttressed by the fact that an issuer independently is subject to the disqualification provisions under Rule 503, as discussed below.[694] In addition, Rule 301(c)(1) implements the requirement of Section 4A(a)(5) that an intermediary conduct a background and securities enforcement regulatory history check on each issuer whose securities are to be offered by the intermediary, as well as on each of its officers, directors (or any person occupying a similar status or performing a similar function) and 20 Percent Beneficial Owners.

While we understand commenters' concerns about the cost of the requirement that intermediaries conduct background checks on issuers and certain affiliated persons, we are not eliminating or limiting the requirement as suggested by commenters because we believe the

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692 *See* StartupValley Letter.

693 *See* Vann Letter.

694 *See* Section II.E.6 (discussing issuer disqualification).

requirement is an important tool for intermediaries to employ when determining whether or not they have a reasonable basis to allow issuers on their platforms. Even though a number of commenters requested that the Commission provide specific requirements for background and securities enforcement regulatory history checks, we are not establishing specific procedures in the final rules. As we indicated in the Proposing Release, we believe that the better approach is to allow an intermediary to be guided by its experience and judgment to design systems and processes to help reduce the risk of fraud in securities-based crowdfunding.[695] We also believe that such flexibility could mitigate cost concerns related to conducting the background and securities enforcement regulatory history checks.

We are not developing a database of denied issuers as suggested by some commenters because we do not believe it would significantly increase investor protection. The requirement to deny an issuer access to a crowdfunding platform under the final rules based on fraud or other investor protection concerns is important to the viability of crowdfunding, and the legitimacy of the intermediary. This obligation is the responsibility of each intermediary, which must make a determination about whether to deny access to an issuer. While a third party may decide to create a database of denied issuers at some point and an intermediary could use such a database to help make its determination as to whether it was required to deny access to an issuer, such a database could not be used as a substitute for an intermediary making its own determination.

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695 We disagree with the commenter that suggested that this method is ineffective because intermediaries lack experience. *See* Consumer Federation Letter. Crowdfunding is a new form of capital formation. We believe broker-dealers and funding portals will gain the relevant experience that will appropriately position them to develop requirements for conducting background checks required by the rule. In addition, we believe that an intermediary's interest in developing a successful platform will motivate it to conduct rigorous background checks.

We also are not requiring an intermediary to make publicly available the results of the background checks or the sources consulted. We believe that the goal of the background check is sufficiently served by the exclusion of an issuer from the intermediary's platform. We do not believe that making the results or sources publicly available adds a significant degree of investor protection under these circumstances, given the potential problems that could arise from such public disclosure of the results, such as the risk of disclosing personally identifiable information or other information with significant potential for misuse. In addition, we are concerned that such requirements could add to the cost of administration and could expose the individuals at the issuer that are subject to a background check to harm, for example, if there were errors in the information made publicly available.

We are adopting Rule 301(c)(2) substantially as proposed, but with certain revisions. As adopted, Rule 301(c)(2) now contains a "reasonable basis" standard as opposed to the initially proposed "believes" standard. Rule 301(c)(2) requires denial of access to its platform when the intermediary has a reasonable basis for believing that the issuer or offering presents the potential for fraud or otherwise raises concerns about investor protection.[696] In a conforming change, Rule 301(c)(2) also requires (i) an intermediary deny access to an issuer if it reasonably believes that it is unable to adequately or effectively assess the risk of fraud of the issuer or its potential offering, and (ii) if the intermediary becomes aware of information after it has granted the issuer access to its platform that causes it to reasonably believe that the issuer or the offering presents the potential for fraud or otherwise raises concerns regarding investor protection, the intermediary must

[696] *See* Section II.D.2. (discussing modified Rule 402(b)(1), which relates to a funding portal's ability to deny access to an issuer).

promptly remove the offering from its platform, cancel the offering and return to investors any funds they may have committed.

We believe that a "reasonable basis" standard is appropriate for Rule 301(c)(2) because it is a more objective standard.[697] Under this standard, an intermediary may not ignore facts about an issuer that indicate fraud or investor protection concerns such that a reasonable person would have denied access to the platform or cancelled the offering. Rule 301(c)(2) is intended to give an intermediary an objective standard regarding the circumstances in which it must act to protect its investors from potentially fraudulent issuers or ones that otherwise present red flags concerning investor protection. This objective standard also will make it easier for an intermediary to assess whether it would be compliant with Rule 301(c)(2) when deciding if it should deny an issuer access or cancel its offering.[698] Thus, we believe these measures likely will promote compliance and help to reduce the risk of fraud with respect to crowdfunding transactions, as required by Section 4A(a)(5). This standard also will provide the Commission with a clear basis to review whether an intermediary's decision not to deny access to its platform or cancel an offering was reasonable given the facts and circumstances.

We are not requiring that an intermediary report the issuers that have been denied access to its platforms, as some commenters suggested, or that the intermediary post a summary of the sources consulted as part of the background check on its platform along with a description of the

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697 Adding the reasonable basis standard to Rule 301(c)(2) also provides a consistent standard across Rule 301, including Rules 301(a), (b) and (c)(1).

698 Aside from the requirement to deny access to issuers under Rule 302(c)(2), it is important to note that intermediaries are permitted to determine whether and under what terms to allow an issuer to offer and sell securities in reliance on Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)) through their platforms. *See* Rule 402(b)(1) and Section II.D.3. The objective standard under Rule 301(c)(2) also helps to clarify that a funding portal would not be providing investment advice or recommendations, if it denies access to or cancels an offering because it has a reasonable basis for believing that there is a potential for fraud or other investor protection concerns. *See* Rule 402(b)(10) of Regulation Crowdfunding and Section II.D.3.i.

intermediary's standards for determining which offerings present a risk of fraud. We also are not adopting a requirement, as suggested by a commenter, that an intermediary notify a potential issuer when the intermediary utilizes third-party information to deny access to the issuer. As with background checks, discussed above, we believe that the investor protection goal is sufficiently served by the exclusion of an issuer from the intermediary's platform. In addition, we are concerned that such requirements could add to the cost of administration and could expose the issuers in question to harm, for example, if there were errors in the information made publicly available. Likewise, we do not believe that requiring an intermediary to post to its website a summary of the sources consulted as part of the background check and a description of the intermediary's standards for determining which offerings present a risk of fraud would sufficiently increase investor protection to justify the burdens, such as those outlined above, that would be associated with imposing such requirements. We also note that providing this information on an intermediary's website may give potentially fraudulent issuers or those that otherwise present investor protection concerns a roadmap to an intermediary's proprietary procedures for screening for fraud that could assist such issuers with impeding or obstructing intermediaries from detecting offerings that present a risk of fraud.

4. Account Opening

a. Accounts and Electronic Delivery

(1) Proposed Rule

Proposed Rule 302(a)(1) of Regulation Crowdfunding would prohibit an intermediary or its associated persons from accepting an investment commitment in a transaction involving the offer or sale of securities in reliance on Section 4(a)(6) unless the investor has opened an account with the intermediary, and the intermediary has obtained from the investor consent to electronic

delivery of materials. Proposed Rule 302(a)(2) would require an intermediary to provide all information required by Subpart C of Regulation Crowdfunding, including, but not limited to, educational materials, notices and confirmations, through electronic means.

Proposed Rule 302(a)(2) also would require an intermediary to provide such information through an electronic message that either contains the information, includes a specific link to the information as posted on the intermediary's platform, or provides notice of what the information is and that it is located on the intermediary's platform or the issuer's website. As proposed, Rule 302(a)(2) stated that electronic messages would include, but not be limited to, messages sent via e-mail.

(2) Comments on the Proposed Rule

One commenter suggested that intermediaries who are brokers should not be required to open new accounts for persons who are existing customers of the broker.[699] In response to our request for comments on whether an intermediary should be required to obtain specific information from investors, and if so what type of information should be required, some commenters generally supported requiring an intermediary to gather specific information from investors, particularly identifying information that could help prevent duplicate or fraudulent accounts and information about other intermediary accounts and investments.[700] A few of these commenters supported the Commission requiring intermediaries to collect investors' social

[699] *See* Arctic Island Letter 2.

[700] *See*, *e.g.*, Consumer Federation Letter; Jacobson Letter; RocketHub Letter.

security numbers.[701] One commenter opposed the Commission requiring intermediaries to obtain particular information from investors.[702]

With respect to electronic delivery, some commenters urged that it should be sufficient for the intermediary simply to make Subpart C materials, such as educational materials, notices and confirmations, available on the intermediary's platform for investors to access.[703] Other commenters broadly opposed permitting intermediaries to satisfy their information delivery requirement by providing an electronic message that informs an investor that information can be found on the intermediary's platform or an issuer's website.[704] One commenter suggested that investors may not actually receive required disclosures because they will not spend the time to find the information.[705] Another commenter suggested that the Commission should "continue to rely instead on the strong and effective policy for electronic delivery of disclosure adopted by the Commission in the mid-1990s."[706] The same commenter noted that it would be "a simple matter to require that any electronic message through which disclosures are delivered include, at a minimum, the specific URL where the required disclosures can be found."[707]

One commenter stated it was concerned that earlier Commission policies on electronic delivery might be read as implying that paper delivery might be permitted in certain

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701 *See, e.g.*, Consumer Federation Letter; RocketHub Letter.

702 *See* Public Startup Letter 3.

703 *See, e.g.*, ASSOB Letter; CrowdCheck Letter 1; RocketHub Letter; Wefunder Letter; Vann Letter.

704 *See, e.g.*, BetterInvesting Letter; AFR Letter; IAC Recommendation; Consumer Federation Letter ("The definition of electronic delivery must be revised to ensure the disclosures themselves, and not just notices of the availability of disclosures, are delivered to investors.").

705 *See* Consumer Federation Letter. *See also* Clapman Letter (suggesting that all issuers and their materials must be "publicly accessible for all investors to have the same opportunity to invest" and stating that "no clubs, or paid to view investment style platforms would therefore be allowed").

706 IAC Recommendation; *see also* BetterInvesting Letter.

707 IAC Recommendation; *see also* BetterInvesting Letter.

circumstances.[708] This commenter did agree, however, that any electronic message through which disclosures are delivered include, at a minimum, the specific URL where the required disclosures can be found.[709]

In response to our request for comments on whether exceptions to the consent to electronic delivery should be allowed, one commenter stated that account creation and delivery of communication should be completed digitally and that there should be no exemption to allow paper delivery as a substitute.[710] Another commenter stated that investors should be allowed to waive these delivery requirements entirely.[711]

(3) Final Rules

After considering the comments, we are adopting as proposed the account opening and electronic delivery requirements in Rule 302(a). We are not prescribing particular requirements for account opening. Rather, we believe that the final rule provides flexibility to intermediaries given that intermediaries are better positioned than the Commission to determine what information and processes it will require, both as a business decision and to ensure compliance with all applicable regulatory requirements. Therefore, for example, an intermediary can decide whether or not to open a new account for an existing customer. We also are not prescribing under the final rule, as a commenter suggested, that an intermediary be required to collect identifying information that could help prevent duplicative or fraudulent accounts. We believe that even without prescribing particular account opening requirements intermediaries should be able to

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708 *See* CFIRA Letter 12.

709 *Id.*

710 *See* RocketHub Letter.

711 *See* Public Startup Letter 3.

identify, by collecting basic account opening information, those accounts that appear to be duplicative or present red flags of potential fraud.

However, the final rules do not permit investors to waive the electronic delivery requirements entirely, as one commenter suggested.[712] We believe that electronic delivery of materials in connection with crowdfunding offerings serves an important and basic investor protection function by conveying information, such as offering materials, that will help investors to make better informed investment decisions and by a method that is appropriately suited to the electronic and Internet-based nature of crowdfunding transactions.

As explained in Section II.A.3, Rule 100(a)(3) of Regulation Crowdfunding requires that crowdfunding transactions be conducted exclusively through an intermediary's platform. Rule 302(a) implements this requirement by requiring that investors consent to electronic delivery of materials in connection with crowdfunding offerings.[713] This requirement applies to all investors, including an existing customer of a registered broker that has not already consented to electronic delivery of materials. Therefore, this requirement will prohibit intermediaries from accepting an investment commitment in a Section 4(a)(6) offering from any investor that has not consented to electronic delivery.

We are adopting substantially as proposed Rule 302(a)(2), which requires that all information required to be provided by an intermediary under Subpart C be provided through electronic means. We have considered the comments but do not believe that it would be sufficient – or consistent with our previous statements about electronic media – for the intermediary simply

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712 *Id.*

713 Certain requirements of Regulation Crowdfunding that require timely actions by issuers and investors will be facilitated by requiring consent to electronic delivery of documents. *See, e.g.,* Section II.C.6 (discussing the five-day periods for investor reconfirmations based on material changes and issuer cancellation notices).

to make Subpart C materials, such as educational materials, notices and confirmations, available on the intermediary's platform for investors to access.[714] Rather, unless otherwise indicated in the relevant rules of Subpart C, [715] the intermediary must provide the information either through (1) an electronic message that contains the information, (2) an electronic message that includes a specific link to the information as posted on the intermediary's platform, or (3) an electronic message that provides notice of what the information is and notifies investors that this information is located on the intermediary's platform or on the issuer's website.[716] We have added to the rule text other examples of electronic messages that are permissible in addition to e-mail messages – specifically text, instant messages, and messages sent using social media.

b. Educational Materials

(1) Proposed Rules

Securities Act Section 4A(a)(3) states that an intermediary must "provide such disclosures, including disclosures related to risks and other investor education materials, as the Commission shall, by rule, determine appropriate," but it does not elaborate on the scope of this requirement. As described in further detail below, proposed Rule 302(b)(1) of Regulation Crowdfunding would

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714 *See Use of Electronic Media*, Release No. 34-42728 (Apr. 28, 2000) [65 FR 25843, 25853 (May 4, 2000)] (discussing the "access equals delivery" concept and citing *Use of Electronic Media for Delivery Purposes*, Release No. 34-36345 (Oct. 6, 1995) [60 FR 53548, 53454 (Oct. 13, 1995)]).

715 For example, Rule 303(a) separately requires that an intermediary must make issuer information publicly available on its platform, and so we do not believe that it is necessary to further require intermediaries to send an electronic message regarding the posting of issuer materials.

716 As noted above, this electronic message could include a specific link to the information as posted on the intermediary's platform. However, we are not requiring intermediaries to provide a link to direct investors to the intermediary's platform or the issuer's website where the information is located. We believe that the final rule provides some flexibility to intermediaries when providing required information through electronic messages given that intermediaries are well-positioned to determine how best to ensure compliance with all applicable regulatory requirements. We also believe that, because of the widespread use of the Internet, as well as advances in technology that allow funding portals to send various electronic messages, our final rule requires sufficient notice to investors.

require intermediaries to deliver to investors, at account opening, educational materials that are in plain language and otherwise designed to communicate effectively and accurately certain specified information. Proposed Rules 302(b)(1)(i)-(viii) would require the materials to include:

- the process for the offer, purchase and issuance of securities through the intermediary;
- the risks associated with investing in securities offered and sold in reliance on Section 4(a)(6);
- the types of securities that may be offered on the intermediary's platform and the risks associated with each type of security, including the risk of having limited voting power as a result of dilution;
- the restrictions on the resale of securities offered and sold in reliance on Section 4(a)(6);
- the types of information that an issuer is required to provide in annual reports, the frequency of the delivery of that information, and the possibility that the issuer's obligation to file annual reports may terminate in the future;
- the limits on the amounts investors may invest, as set forth in Section 4(a)(6)(B);
- the circumstances in which the issuer may cancel an investment commitment;
- the limitations on an investor's right to cancel an investment commitment;
- the need for the investor to consider whether investing in a security offered and sold in reliance on Section 4(a)(6) is appropriate for him or her; and
- that following completion of an offering, there may or may not be any ongoing relationship between the issuer and intermediary.

Proposed Rule 302(b)(2) would further require intermediaries to make the current version of the educational materials available on their platforms, and to make revised materials available to all

investors before accepting any additional investment commitments or effecting any further transactions in securities offered and sold in reliance on Section 4(a)(6).

(2) Comments on Proposed Rules

Commenters generally supported distribution of educational materials through intermediaries.[717] Some stated that intermediaries should be required to submit educational materials to the Commission or to FINRA because oversight and review is needed for materials that will be used by unsophisticated investors,[718] while others stated that intermediaries should not be required to submit educational materials to the Commission or to FINRA because it would be cumbersome and expensive.[719] One commenter stated that the proposed requirements should be modified to state that education must be done prior to an investor's first investment in a Section 4(a)(6) offering, not at account opening.[720]

Some commenters suggested that additions be made to the scope of information proposed to be required in an intermediary's educational materials,[721] to include information about exit strategies;[722] principles of investing in crowdfunding and how to evaluate investment

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717 *See*, *e.g.*, Arctic Island Letter 6; CFA Institute Letter; Cole Letter; Consumer Federation Letter; Gimpelson Letter 2; Heritage Letter; Jacobson Letter; NSBA Letter; Patel Letter; RocketHub Letter; STA Letter; StartupValley Letter; Wefunder Letter.

718 *See*, *e.g.*, Consumer Federation Letter; Gimpelson Letter 2; Jacobson Letter. *See also* RocketHub Letter (stating that "if educational materials are submitted to the Commission for approval, such approval should act to limit liability of the Portal under the Act").

719 *See*, *e.g.*, Arctic Island Letter 6; Joinvestor Letter; StartupValley Letter; Wefunder Letter.

720 *See* Arctic Island Letter 6. The commenter also stated that the educational material requirements should only apply to unaccredited investors, but we note that the requirement under Section 4A(a)(4) runs to "each investor." As discussed above, we believe that Congress intended for crowdfunding transactions under Section 4(a)(6) to be available equally to all types of investors. Consistent with that approach, we do not believe at this time it would be appropriate to tailor the educational requirements for any particular type of investor or to create an exemption for accredited investors. Further, issuers can rely on other exemptions to offer and sell securities to accredited investors or institutional investors.

721 *See*, *e.g.*, Anonymous Letter 1; Gimpelson Letter 2; RocketHub Letter; STA Letter; Angel Letter 1.

722 *See* Anonymous Letter 1.

opportunities in privately held companies;[723] the risks associated with crowdfunding investments;[724] and reasons for investors to maintain their own personal records concerning crowdfunding investments.[725] One commenter suggested that educational materials "should include an industry standard disclosure document on the benefits and risks of crowdfunding investments."[726] This commenter indicated that "having these generic risk factors in the industry standard educational materials will help focus the company specific disclosure on the factors that are most important."[727]

Some commenters suggested that intermediaries should be required to design questionnaires to increase investor knowledge and to monitor whether investors actually access materials.[728] One commenter suggested that in addition to an "interactive questionnaire," the Commission should also "require that investors reaffirm each time they invest that they understand the risks associated with crowdfunding, can afford to lose their entire investment, and do not expect to need the funds being invested in the near term."[729]

Some commenters stated that we should develop model educational materials for investors or specify the content for intermediaries.[730] One commenter suggested that the Commission, state

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723 *See* Gimpelson Letter 2.

724 *See* RocketHub Letter.

725 *See* STA Letter.

726 *See* Angel Letter 1.

727 *Id*. (suggesting an issuer-specific disclosure document).

728 *See*, *e.g*., AFR Letter; BetterInvesting Letter; Consumer Federation Letter; IAC Recommendation. One commenter also suggested requiring intermediaries to post a list of previous offerings on their web sites with information about the offerings. *See* Angel Letter 1.

729 IAC Recommendation; *see also* BetterInvesting Letter.

730 *See*, *e.g*., CFA Institute Letter; Guzik Letter 1; Heritage Letter; Jacobson Letter; Joinvestor Letter; NSBA Letter; STA Letter. *See also* CfPA Letter (stating that guidance on the requirements for educational materials and certification of compliance should be created and administered by an industry-related body with approval and oversight by the Commission).

securities regulators, and FINRA, together, should develop "a sample guide" designed to alert investors to the risks of crowdfunding including, among other things, "the high failure rate of small startup companies, the fact that shares will not be set based on market data and may therefore be mispriced, the lack of liquidity, and the risk that, absent appropriate protections, the value of their shares could be diluted."[731] This commenter also suggested that the guide "should include explicit warnings that investors should not invest in crowdfunding unless they can afford to lose the entire amount of their investment or if they expect to have an immediate need for the funds."[732] This commenter also stated that regulators should test the materials with investors to ensure their effectiveness.[733]

One commenter stated that we should not limit or specify the type of electronic media being used to communicate educational material.[734] Finally, one commenter opposed all the educational requirements for intermediaries, and suggested instead that the Commission itself, rather than intermediaries, should provide investor educational materials to both investors and issuers with funding portals linking to, for example, the SEC webpage or an open source website containing any Commission drafted educational materials.[735]

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731 IAC Recommendation; *see also* BetterInvesting Letter.

732 *Id*.

733 *Id*. (suggesting that the Commission should take additional steps "to strengthen requirements with regard to content and delivery of educational materials in order to increase the likelihood both that they will be read and that they will clearly convey the essential information"); *see also* CFIRA Letter 12 (agreeing with IAC's suggestion that the Commission "could establish a set of standard educational requirements for the industry that could be adopted by intermediaries").

734 *See* Gimpelson Letter 2.

735 *See* Public Startup Letter 3.

(3) Final Rules

After considering the comments, we are adopting Rule 302(b) relating to educational materials substantially as proposed, but adding one further requirement as to the content of the materials. We believe that, consistent with Section 4A(a)(3) it is appropriate that intermediaries, rather than the Commission (as a commenter suggested), be required to provide such disclosures, including disclosures related to risks and other investor education materials as the Commission determines to be appropriate. We believe that intermediaries are better equipped and positioned, as compared to the Commission, to provide educational materials to investors that are reasonably tailored to an intermediary's offerings and investors, particularly in light of their access to and interactions with investors.

We further believe that the scope of information that we are requiring to be included in an intermediary's educational materials is appropriate. In the Proposing Release we discussed our rationales for requiring the different types of disclosures in the educational materials. As we noted in the Proposing Release, we generally drew upon the statutory provisions when including disclosures required in the educational materials relating to the risks of investing in securities offered and sold in reliance on Section 4(a)(6), investors' cancellation rights, resale restrictions and issuer reporting.[736] The circumstances in which an investor can cancel an investment commitment and obtain a return of his or her funds are particularly important to an investor's understanding of the investment process and may affect an investor's decision to consider any offerings made pursuant to Section 4(a)(6). The items required to be included, pursuant to Rule 302(b)(1)(i) through (viii), in the educational materials are basic terms, relevant to transactions conducted in reliance on Section 4(a)(6), of which all investors should be aware before making an

[736] *See* Securities Act Sections 4A(a)(4), 4A(a)(7), 4A(e), and 4A(b)(4).

investment commitment. Furthermore, information on the various types of securities that can be available for purchase on the intermediary's platform, any applicable resale restrictions, and the risks associated with each type of security, including the risk of having limited voting power as a result of dilution can affect an investor's decision to consider any offerings made pursuant to Section 4(a)(6). In addition, we are adding Rule 302(b)(1)(ix) to require the educational materials to indicate that under certain circumstances an issuer may cease to publish annual reports and, therefore, an investor may not continually have current financial information about the issuer. We are adding this requirement because we believe that it is important for investors to be able to consider the ongoing availability of information about an issuer's financial condition when they assess whether to invest in that issuer.

The final rule provides each intermediary with sufficient flexibility to determine: (1) the content of the educational materials, outside of the minimum specified information required to be included under Rule 302(b)(1)(i)-(viii), and (2) the overall format and manner of presentation of the materials. We believe this flexibility will allow the intermediary to prepare and present educational materials in a manner reasonably tailored to the types of offerings on the intermediary's platform and the types of investors accessing its platform. While we have determined not to provide model educational materials, impose additional content (beyond those proposed) or format requirements, mandate particular language or manner of presentation, or require that an intermediary design an investor questionnaire, as suggested by commenters, the final rules do not prohibit an intermediary from providing additional educational materials if they choose. For example, because the final rules do not require an intermediary to design a questionnaire, intermediaries maintain the flexibility in meeting the rule's requirements to determine whether such a disclosure format would be cost effective and appropriate particularly in

light of that intermediary's particular business model. We further note the suggestion by some commenters that we require additional information in the educational materials, including, for example, requiring an intermediary to discuss exit strategies, how to evaluate investment opportunities in privately held companies, and the reasons for investors to maintain their own personal records concerning crowdfunding investments. Although these suggestions may provide investors with some useful information, we are not persuaded that imposing such additional requirements in the final rule is necessary at this time as it is unclear that those suggestions would significantly strengthen the investor protections that will result from Rule 302(b) as adopted. We also believe that adding such requirements may overly complicate these educational materials and increase the costs associated with preparing them. Therefore, we have determined to allow intermediaries the flexibility to prepare educational materials reasonably tailored to their offerings and investors, provided the materials meet the standards and include the information required to be provided under Rule 302(b).[737]

We also recognize that FINRA or any other registered national securities association may implement additional educational materials requirements. We are not, however, as one commenter suggested,[738] requiring at this time that intermediaries submit their educational materials to the Commission or to a registered national securities association for review and approval. We note, however, that a registered national securities association could propose such a requirement as its oversight of intermediaries in this new market evolves. Any such proposed

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[737] We note that educational materials may be subject to examination and inspection. *See* Section II.D.5. (describing the recordkeeping obligations of funding portals).

[738] *See* RocketHub Letter (stating that "if educational materials are submitted to the Commission for approval, such approval should act to limit liability of the Portal under the Act").

requirement would be considered by the Commission, and subject to public notice and opportunity for comment, pursuant to Exchange Act Section 19(b) and Rule 19b-4.

Rule 302(b)(2) requires an intermediary to keep its educational materials accurate. Accordingly, an intermediary must update the materials as needed to keep them current. In addition, if an intermediary makes a material revision to its educational materials, the rule requires that the intermediary make the revised educational materials available to all investors before accepting any additional investment commitments or effecting any further crowdfunding transactions. An intermediary will also be required to obtain a representation that an investor has reviewed the intermediary's most recent educational materials before accepting an investment commitment from the investor.[739]

We believe that these requirements will benefit investors by helping to ensure that they receive information about key aspects of investing through the intermediary's platform, including aspects that may have changed since the last time they received the materials, prior to making investment commitments, as that information can influence their investment decisions. We also believe that requiring intermediaries to update materials on an ongoing basis, rather than at certain specified intervals, will help to ensure that those materials are updated as circumstances warrant, which, in turn, will provide investors with more current information and increase investor protection.

c. Promoters

(1) Proposed Rule

Securities Act Section 4A(b)(3) provides that an issuer shall "not compensate or commit to compensate, directly or indirectly, any person to promote its offerings through communication

[739] *See* Rule 303(b)(2)(i) of Regulation Crowdfunding.

channels provided by a broker or funding portal, without taking such steps as the Commission shall, by rule, require to ensure that such person clearly discloses the receipt, past or prospective, of such compensation, upon each instance of such promotional communication." Under Rule 205 of Regulation Crowdfunding, as discussed above, an issuer can compensate persons to promote its offerings through communications channels provided by the intermediary on its platform, where certain conditions are met.[740]

We separately proposed in Rule 302(c) of Regulation Crowdfunding to require the intermediary to inform investors, at the account opening stage, that any person who promotes an issuer's offering for compensation, whether past or prospective, or who is a founder or an employee of an issuer that engages in promotional activities on behalf of the issuer on the intermediary's platform, must clearly disclose in all communications on the platform the receipt of the compensation and the fact that he or she is engaging in promotional activities on behalf of the issuer.

(2) Comments on Proposed Rules

Some commenters suggested that the promoter disclosures should not be made at account opening where they may be ignored.[741] One commenter proposed that the disclosures should be made "prior to any participant on the platform being able to post comments, reviews, ratings, or other promotional activities."[742]

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740 *See* Rule 205 of Regulation Crowdfunding and the discussion in Section II.B.5.

741 *See*, *e.g.*, Arctic Island Letter 6; Wefunder Letter.

742 *See* Arctic Island Letter 6.

(3) Final Rules

We are adopting, as proposed, Rule 302(c) requiring intermediaries to inform investors, at the time of account opening, that promoters must clearly disclose in all communications on the platform the receipt of the compensation and the fact that he or she is engaging in promotional activities on behalf of the issuer. As noted in the Proposing Release, in addition to the information required under Rule 302(c), promoters will also be required to comply with Section 17(b) of the Securities Act, which requires promoters to fully disclose to investors the receipt, whether past or prospective, of consideration and the amount of that compensation.[743] We believe that the disclosures required by Rule 302(c) will help alert investors at the outset, rather than after the account is opened, of the fact that information about the promotional activities of issuers or representatives of issuers will be disclosed at a later time on the platform, pursuant to Rule 303(c)(4). We believe that the account opening is the appropriate time for this disclosure because it gives investors notice of potential promotional activities by issuers and their representatives prior to making investment commitments. As discussed below, Rule 303(c)(4) separately mandates that intermediaries require any person, when posting a comment in the communication channels, to clearly disclose with each posting whether he or she is a founder or an employee of an issuer engaging in promotional activities on behalf of the issuer, or receives compensation, whether in the past or prospectively, to promote an issuer's offering. We believe that the disclosure requirements of Rule 302(c), when coupled with the additional disclosure requirements in Rule 303(c)(4), will promote a transparent information sharing process whereby investors are able to discern the sources of information that they are receiving and any potential conflicts of interest by those sources.

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[743] *See* Proposing Release at 78 FR 66467-68. *See also* Section 17(b) of the Securities Act (15 U.S.C. 77q(b)).

d. Compensation Disclosure

(1) Proposed Rule

Proposed Rule 302(d) of Regulation Crowdfunding would require that intermediaries, when establishing an account for an investor, clearly disclose the manner in which they will be compensated in connection with offerings and sales of securities made in reliance on Section 4(a)(6). This requirement would help to ensure investors are aware of any potential conflicts of interest that may arise from the manner in which the intermediary is compensated. Rule 201(o) of Regulation Crowdfunding, which is discussed in Section II.B.1, separately requires an issuer to disclose in its offering materials, among other things, the amount of compensation paid to the intermediary for conducting a particular offering, including the amount of referral and any other fees associated with the offering.

(2) Comments on Proposed Rule

Several commenters supported the disclosure of intermediary compensation.[744] One commenter stated that the account opening is not an appropriate time to mention compensation, asserting that the account opening stage should be dedicated to discussing the risk of startup investing.[745] One commenter suggested that the best way for an intermediary to disclose compensation is through a "Costs and Fees" page on its website.[746] Another commenter requested that the Commission define compensation as any fees or compensation collected by the

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744 *See*, *e.g.*, Arctic Island Letter 6; ASSOB Letter; CFA Institute Letter; Commonwealth of Massachusetts Letter; Joinvestor Letter; StartupValley Letter; Wefunder Letter.

745 *See* Wefunder Letter.

746 *See* StartupValley Letter.

intermediary in connection with a Section 4(a)(6) transaction, subject to Commission and FINRA rules.[747]

(3) Final Rules

We are adopting Rule 302(d) as proposed. We believe that requiring intermediaries to provide information to investors about the manner in which they will be compensated at account opening, rather than at a subsequent time, will provide investors with notice of how the intermediary is being compensated at a threshold stage in the relationship (*i.e.*, account opening), which, in turn, will help investors make better-informed decisions. We note that the final rules – unlike the proposed rules – allow intermediaries to receive a financial interest in the issuer as compensation, subject to certain limitations.[748] Therefore, an intermediary that receives or may receive a financial interest in an issuer in the future as compensation for its services is required to disclose that compensation at account opening. We also note that Rule 201(o), which is discussed in Section II.B.1 and separately requires an issuer to disclose in its offering materials a description of the intermediary's interests in the issuer's transaction, including the amount of compensation paid or to be paid to the intermediary for conducting a particular offering, the amount of referral and any other fees associated with the offering. We are not defining compensation as one commenter suggested, as we believe the final rule's requirement to clearly disclose the manner in which an intermediary will be compensated in connection with offerings and sales of securities made in reliance on Section 4(a)(6) is sufficiently clear, and because we are also concerned that a definition of compensation could be both under- and over-inclusive in a new and evolving crowdfunding market.

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747 *See* CFIRA Letter 4.

748 *See* Section II.C.2.b.

5. Requirements with Respect to Transactions

a. Issuer Information

(1) Proposed Rule

Securities Act Section 4A(a)(6) requires each intermediary to make available to the Commission and investors, not later than 21 days prior to the first day on which securities are sold to any investor (or such other period as the Commission may establish), any information provided by the issuer pursuant to Section 4A(b).[749] Accordingly, we proposed Rule 303(a) of Regulation Crowdfunding to implement this provision by requiring each intermediary in a transaction involving the offer or sale of securities in reliance on Section 4(a)(6) to make available to the Commission and to investors any information required to be provided by the issuer under Rules 201 and 203(a) of proposed Regulation Crowdfunding. As proposed, Rule 303(a) would require that this information: (1) be publicly available on the intermediary's platform, in a manner that reasonably permits a person accessing the platform to save, download or otherwise store the information; (2) be made publicly available on the intermediary's platform for a minimum of 21 days before any securities are sold in the offering, during which time the intermediary may accept investment commitments; and (3) remain publicly available on the intermediary's platform until the offer and sale of securities is completed or cancelled (including any additional information provided by the issuer). In addition, under Proposed Rule 303(a)(4), an intermediary would be prohibited from requiring any person to establish an account with the intermediary in order to access this information.

[749] As discussed in Section II.B, Securities Act Section 4A(b) establishes the requirements for an issuer that offers or sells securities in reliance on Section 4(a)(6).

(2) Comments on the Proposed Rule

Several commenters suggested that so long as issuer information is made available on the intermediary's platform, the rules should not mandate the delivery of this information, in addition to or in lieu of, making the information available on the intermediary's platform.[750]

One commenter stated that having information about a deal publicly available on the intermediary's website will increase the potential for fraud—specifically, potential fraud involving "data scraping" from websites (*i.e.*, copying data from these websites in order to use that data for fraudulent purposes).[751] This same commenter suggested that that there should be two levels of disclosure: the first, would be available to all and would contain certain general information about the issuer and the terms of deal, and the second would be made available only after investors proceed through a membership registration process and would contain disclosure documents, financial information, legal disclosures and further information.[752]

As to the amount of time that an intermediary should display issuer materials prior to the first day on which securities are sold to any investor, some commenters supported the 21-day time frame as a sufficient minimum period that offering information should be made available through the intermediary's platform.[753]

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750 *See*, *e.g.*, Arctic Island Letter 6 (suggesting that an electronic copy of the signed subscription agreement and risk disclosures should be sent to the investor via email, and that "[e]verything else can be referenced by the investor online at any time"); ASSOB Letter; CrowdCheck Letter (suggesting that the Commission remove the requirement in the proposed rules that would effectively limit the presentation of information to only formats that can be saved and downloaded by prospective investors); RocketHub Letter; Wefunder Letter; Vann Letter (stating that no particular means of delivery to investors should be required because "technologies may change" and intermediaries should be allowed to use whatever means "appropriate").

751 *See* StartupValley Letter.

752 *Id*. *See also* Early Shares Letter (suggesting a permission-based system for the disclosure of certain "sensitive" information about the offering).

753 *See*, *e.g.*, ASSOB Letter; RocketHub Letter.

Although one commenter objected to intermediaries displaying any issuer materials,[754] several commenters supported requiring intermediaries to continue to display issuer materials for some period of time after completion of the offering.[755] One commenter, however, stated that intermediaries should not be required to display issuer materials for closed offerings.[756] Another commenter stated that "[o]nce an offering is complete, an issuer should have the right to limit publicly available information." [757]

We also requested comments as to whether an intermediary should make efforts to ensure that an investor has actually reviewed the relevant issuer information. A few commenters expressed concern with requiring intermediaries to ensure that an investor has reviewed the relevant issuer information.[758] Another commenter suggested that an investor "should demonstrate, through a representation of acknowledgment, that they have reviewed all relevant issuer information."[759]

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754 *See* Public Startup Letter 3.

755 *See*, *e.g.*, Arctic Island Letter 6 (stating that an issuer's offering materials should be permanently displayed so it can easily be referenced in the future); ASSOB Letter (suggesting a period of at least two years after receiving funding from the offering); Jacobson Letter (suggesting a period of at least six years after an offering closes); RocketHub Letter (recommending that issuer materials should remain displayed for an additional 30 days after completion of the offering and further suggesting that "[i]ntermediaries should have the right, at their own discretion, to continue to display the entire offering, or parts of it, for as long as they see fit").

756 *See* Whitaker Chalk Letter (stating that removing such materials from the intermediary's platform would prevent the public from relying on "stale" information and opposing the requirement that intermediaries keep public any such "stale" information so long as the information remain subject to the intermediary's recordkeeping requirements).

757 *See* RocketHub Letter.

758 *See*, *e.g.*, Arctic Island Letter 6 (stating that such a requirement "could make things incredibly messy and expensive"); Wefunder Letter.

759 RocketHub Letter.

(3) Final Rules

After considering the comments, we are adopting, as proposed, Rule 303(a). As stated in the Proposing Release, we believe that the requirement in Rule 303(a) that the information must be made publicly available on the intermediary's website satisfies the requirement under Section 4A(d) for the Commission to "make [available to the states], or . . . cause to be made [available] by the relevant broker or funding portal, the information" issuers are required to provide under Section 4A(b) and the rules thereunder. Moreover, this approach should help investors, the Commission, FINRA (and any other applicable registered national securities association) and other interested parties, such as state regulators, to access information without impediment. Therefore, we believe that this rule is not only consistent with the statute but that it also enhances investor protection by having issuer information about a crowdfunding security publicly available on the intermediary's website. While we considered the concern expressed by one commenter that having such information available on the intermediary's website would increase the potential for "data scraping,"[760] we believe the expected benefits of the requirement to investors and other interested persons, as discussed above, justifies the risk of potential harm from such potential activities.

We note that commenters who addressed the issue generally supported a 21-day time frame as the minimum period that offering information should be made available through the intermediary's platform prior to the first day on which securities are sold to any investor. Under the final rules, the information must remain available on the platform until the offering is completed or canceled. While some commenters suggested that the rule should require intermediaries to continue to display issuer materials for some period of time after completion of

[760] *See* StartupValley Letter.

the offering, we are not prescribing such a requirement nor are we prohibiting intermediaries from doing so if they so choose. Although we appreciate that historical issuer information may provide helpful background for investors generally, we are concerned that imposing such a requirement could potentially result in persons relying on potentially stale issuer information particularly given the nature of the crowdfunding market (*i.e.*, we assume that each issuer generally will conduct only one offering per year).[761] We note that intermediaries nonetheless are required to retain the information in accordance with their obligation to make and preserve for a period of time records with respect to any written materials that are used as part of an intermediary's business, including issuer materials made available on their platforms.[762]

While the intermediary plays an important gatekeeper function, the investor has responsibility for his or her actions as well. To that end, we are not requiring that an intermediary ensure that an investor has actually reviewed the relevant issuer information. We believe that the requirements of Rule 303(a) provide an investor with the relevant issuer information and an adequate period of time in which to evaluate the investment opportunity before investing. We are not at this time imposing additional requirements on the intermediary in this regard.

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[761] As discussed in Section IV.B.1, we assume, for purposes of the Paperwork Reduction Act, that each issuer will conduct one offering per year.

[762] Registered brokers would have to maintain records pursuant to Exchange Act Section 17 and the rules thereunder. 15 U.S.C. 78q; 17 CFR 240.17a *et seq*. Funding portals would be subject to the recordkeeping requirements of proposed Rule 404 of Regulation Crowdfunding. *See* Section II.D.5 (discussing the recordkeeping requirements we are adopting for funding portals).

b. Investor Qualification

(1) Compliance with Investment Limits

(a) Proposed Rule

Securities Act Section 4(a)(6)(B) limits the aggregate amount of securities that can be sold by an issuer to an investor in reliance on Section 4(a)(6) during a 12-month period. Securities Act Section 4A(a)(8) requires that intermediaries "make such efforts as the Commission determines appropriate, by rule" to ensure that no investor has made purchases in the aggregate, from all issuers, that exceed the limits in Section 4(a)(6).

Proposed Rule 303(b)(1) of Regulation Crowdfunding would implement this latter provision by requiring that, each time before accepting an investment commitment on its platform (including any additional investment commitment from the same person), an intermediary must have a reasonable basis for believing that the investor satisfies the investment limits established by Section 4(a)(6)(B). The proposed rule would allow an intermediary to rely on an investor's representations concerning annual income, net worth and the amount of the investor's other investments in securities sold in reliance on Section 4(a)(6) through other intermediaries unless the intermediary has a reasonable basis to question the reliability of the representation.

(b) Comments on the Proposed Rule

A number of commenters supported the proposed requirements for enforcing investment limits and intermediary responsibility for investor compliance,[763] while a few commenters

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[763] *See, e.g.*, BetterInvesting Letter; CFA Institute Letter; CFIRA Letter 12; Finkelstein Letter; IAC Recommendation; Milken Institute Letter. *See also* NAAC Letter (stating that unsophisticated investors might not comply with the investment limits or be targets for fraudulent schemes, and recommending "verified and stringent determinations as to the income and net worth qualifications of any potential investors.").

opposed the requirements.[764] Several commenters suggested ways to strengthen the requirements, such as by: requiring that an intermediary conduct more stringent checks,[765] having the Commission maintain a registry of those who have purchased crowdfunding securities,[766] requiring that investors electronically upload financial documents for verification of income or net worth,[767] requiring notices detailing investment limits and highlighting their importance,[768] and precluding an investor who violates the investment limits from bringing a cause of action against an issuer.[769] Some commenters suggested that the Commission require intermediaries to create a tool for investors to use, such as a questionnaire, to assemble the underlying data on which investment limits are calculated and to perform those calculations electronically.[770] However, another commenter disagreed with this suggestion.[771] One commenter suggested intermediaries' platforms be required to provide to investors prior to accepting an investment commitment a detailed statement of the investment limits that are applicable to investors that also includes a

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764 *See, e.g.*, Moskowitz Letter (stating that select investors on the secondary market could purchase shares in excess of the investment limit and suggesting that the limits be removed altogether); Phillips Letter.

765 *See, e.g.*, Moskowitz Letter; NAAC Letter.

766 *See* Clapman Letter. *See also* CFA Institute Letter (suggesting that the Commission require intermediaries to "cross check each investor's information against other files on record with the Commission to ensure compliance with the law's limitations").

767 *See, e.g.*, Consumer Federation Letter; Finkelstein Letter.

768 *See* Milken Institute Letter.

769 *Id*.

770 *See, e.g.*, CFA Institute Letter (suggesting that "investors be required to complete online questionnaires denoting the different classes of asset holdings permitted by the law, with a specific and prominent notification that the value of one's primary residence is excluded"); IAC Recommendation (stating that the tool, such as an electronic work sheet, would assist investors in identifying categories of assets and liabilities such as bank accounts, investment accounts, and house value, for purposes of the net worth calculation, and prompt them to deduct outstanding liabilities and exclude the value of principle residence). *See also* BetterInvesting Letter.

771 *See* CFIRA Letter 12 (disagreeing with IAC's suggestion "that portals create a 'tool' to walk investors through the creation of what is essentially a personal balance sheet").

penalty of perjury certification by the investor.[772] A few commenters emphasized a need to warn investors that the value of their primary residence should be excluded for purposes of the net worth calculation.[773] Commenters also suggested that the Commission adopt an approach similar to that under the capital gains tax rules that would limit benefits and loss recovery for investors who invest outside of their limits.[774]

Several commenters opposed the proposal to allow an intermediary to rely on the representations of an investor.[775] Some urged the Commission to provide for verification through either a third-party service or through the intermediaries themselves in lieu of reliance on investor representations.[776] Other commenters suggested that intermediaries should be required to take certain affirmative steps to verify investor representations.[777] One commenter stated that the strongest possible approach to a verification requirement should be imposed for investments beyond $2,000.[778] Another commenter suggested that the Commission create penalties for

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772 *See* Milken Institute Letter ("This would underscore the importance of the investor caps . . . and properly place the burden of compliance on the actor who can verify income or wealth at the lowest cost -- the investor.").

773 *See*, *e.g.*, Brown J. Letter; CFA Institute Letter; Consumer Federation Letter.

774 *See*, *e.g.*, Milken Institute Letter (supporting the proposed investment caps, but agreeing with precluding loss recovery); Phillips Letter.

775 *See*, *e.g.*, Accredify Letter (stating that self-certifications are not an effective way to implement the investment limit requirements and suggesting that intermediaries be required to use existing services to check individuals' investment limits); AFL-CIO Letter; AFR Letter; Brown J. Letter; Commonwealth of Massachusetts Letter; Consumer Federation Letter; Farnkoff Letter; Letter Finkelstein Letter; Jacobson Letter; Merkley Letter (noting that permitting self-certification would expose investors to precisely the risks that the statute aimed to prevent, and should not be permitted for investments over $2,000); Saunders Letter; Verinvest Letter.

776 *See*, *e.g.*, Accredify Letter; Commonwealth of Massachusetts Letter; Farnkoff Letter ("A third-party verification regime overseen by the SEC or FINRA would provide the safest protection from fraudsters and reduce risks of liability for funding portals."); Saunders Letter; Verinvest Letter.

777 *See*, *e.g.*, AFL-CIO Letter; Jacobson Letter.

778 *See* Merkley Letter (suggesting that the Commission could reconsider possible options to relax any strict initial approach after the first few years of the final rules being in effect, and stating that "it would be incredible if the verification requirements for ordinary investors in crowdfunding were permitted to be less than for accredited investors under Rule 506(c)").

intermediaries who fail to meet their duties regarding investment limits.[779] One commenter suggested the Commission should require crowdfunding portals to collect enough data from investors to avoid the most likely errors in calculating the investment limit and to prevent evasion of those limits. This commenter also suggested that the Commission should require portals to collect social security numbers to help prevent individuals from evading limits by opening multiple accounts under false names.[780]

Other commenters supported the proposal to allow an intermediary to rely on the representations of an investor.[781] Some of these commenters warned against costly compliance requirements such as, for example, requiring verification of investment limits by both the issuer and the intermediary,[782] or burdening a broker-dealer with a vetting requirement for someone who may only want to invest a small amount, such as $25.[783]

Several commenters supported requiring an intermediary to confirm investment limits compliance using a centralized database, should one become established.[784] A number of these commenters suggested the database be created and managed by the Commission with mandatory intermediary participation[785] to allow intermediaries to check an investor's total year to date

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779 *See* Commonwealth of Massachusetts Letter.

780 *See* AFR Letter.

781 *See*, *e.g.*, Arctic Island Letter 6; ASSOB Letter; CFA Institute Letter; Greenfield Letter; Heritage Letter; Joinvestor Letter; Patel Letter; Public Startup Letter 3; RocketHub Letter.

782 *See* Heritage Letter.

783 *See* Arctic Island Letter 6.

784 *See*, *e.g.*, BetterInvesting Letter; Arctic Island Letter 6; Consumer Federation Letter; Finkelstein Letter; IAC Recommendation; Merkley Letter; Verinvest Letter. *See also* CFA Institute Letter (suggesting that "the Commission require such intermediaries to cross check each investor's information against other files on record with the Commission to ensure compliance with the law's limitations").

785 *See*, *e.g.*, Arctic Island Letter 6; Consumer Federation Letter; Finkelstein Letter. *See also* CFA Institute Letter.

purchases across all platforms.[786] One commenter stated that the statute "contemplates" the development of a central data repository and suggested that it could be established at the relevant national securities association.[787] Another commenter suggested, in connection with its support for the use of a centralized database, imposing a three-to-five year time limit, after which intermediaries would no longer be permitted to rely on investor representations about their investments on other platforms.[788] One commenter suggested the Commission incentivize the private creation of a centralized database.[789] Another opposed the Commission imposing any obligation on intermediaries until after such a centralized database is established.[790] Another commenter, supporting the creation of a single, centralized database, warned that "competing databases" would be incomplete.[791]

Others commenters expressed concern that the proposed rule included no mechanism to prevent investors from registering with multiple platforms and investing far in excess of the statutory limits.[792] Commenters who addressed the issue supported requiring intermediaries to request information about any other intermediary accounts prior to accepting an investment

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786 *See* Finkelstein Letter.

787 *See* Merkley Letter (noting that the proposal "does not establish such a repository or set forth any path towards its establishment and thus fails to implement the plain meaning of the statutory language" and suggesting that "[t]esting, supervisory oversight, and other mechanisms to ensure investors are protected . . . be more fully considered").

788 *See* Consumer Federation Letter.

789 *See* IAC Recommendation (suggesting the Commission create such an incentive by monitoring the effectiveness of the proposed reasonable reliance approach and to end that approach if a cost-effective and suitable cross-portal monitoring system is developed); *see also* BetterInvesting Letter.

790 *See* Wefunder Letter.

791 *See* CFIRA Letter 12.

792 *See*, *e.g.*, Finkelstein Letter; Vann Letter (stating that intermediaries should be required to "make it clear that the aggregate limits apply across all such platforms, not just their own").

commitment.[793] One of these commenters suggested requiring intermediaries to add a text box to their site that requires the investor to input the total dollar amount invested on other platforms.[794] The other commenter stated that an intermediary should only be required to request additional information if there are doubts about the investor's self-certification.[795]

(c) Final Rules

After considering the comments, we are adopting Rule 303(b)(1) as proposed. As a threshold matter, we note that a number of commenters supported the proposed approach for establishing compliance with investment limits. Although we appreciate some of the additional suggestions provided by commenters, as outlined above, we believe the approach in Rule 303(b)(1) for establishing compliance with investment limits is an appropriate means of implementing the provisions of Section 4A(a)(8), which is designed to help ensure that an investor has not made purchases, in the aggregate from all issuers, that exceed those limits during a 12-month period. We note, however, that intermediaries can, in their discretion, take additional measures for evaluating investors' compliance with investment limits, including those suggested by commenters, such as: using a centralized data repository, to the extent that one is created; requiring verification of income or net worth electronically by uploading financial documents; or creating a tool for investors to use, such as a questionnaire, to assemble the underlying data.

While several commenters opposed permitting an intermediary to rely on the representations of an investor about investment limits and some suggested requiring intermediaries to take certain affirmative steps to verify compliance, we believe that it would be

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793 *See*, *e.g*., ASSOB Letter; Wefunder Letter.

794 *See* Wefunder Letter.

795 *See* ASSOB Letter.

difficult for intermediaries to monitor or independently verify whether each investor remains within his or her investment limits where the investor may be participating in offerings on multiple platforms. We note, however, that reliance on investor representations must be reasonable. At a minimum, it would not be reasonable, and therefore would be a violation of the rule and potentially subject to an enforcement action by the Commission, for an intermediary to ignore investments made by an investor in other offerings on the intermediary's platform, to not obtain information and take into account investments made by an investor in other offerings (made in reliance on Section 4(a)(6)) on platforms that are controlled by or under common control with the intermediary, or to ignore other information or facts about an investor within its possession.

Under the final rules, an intermediary will be permitted to reasonably rely on a centralized data repository of investor information, should one be created in the future. We are not mandating the creation of such a database at this time, in part to help to minimize the obstacles that intermediaries may face in getting this newly formed marketplace up and running.[796] We note, in response to one commenter,[797] that it is the Commission's normal practice to review the effectiveness of all of its rules, particularly in light of market developments, and consider changes as the Commission deems appropriate. Commission staff expects to review the need for a

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[796] We do not believe that the statute requires the establishment of a centralized database or repository of investor information as one commenter suggested. *See* Merkley Letter. Instead, the statute calls for intermediaries to "make such efforts as the Commission determines appropriate, by rule" to ensure that no investor exceeds the investment limits set forth in Section 4(a)(6).

[797] *See* IAC Recommendation; *see also* BetterInvesting Letter.

centralized database during the study of the federal crowdfunding exemption that it plans to undertake no later than three years following the effective date of Regulation Crowdfunding.[798]

(2) Acknowledgment of Risk

(a) Proposed Rule

Securities Act Section 4A(a)(4) requires an intermediary to ensure that each investor: (1) reviews educational materials; (2) positively affirms that the investor understands that he or she is risking the loss of the entire investment and that the investor could bear such a loss; and (3) answer questions demonstrating an understanding of the level of risk generally applicable to investments in startups, emerging businesses and small issuers, the risk of illiquidity and such other matters as the Commission determines appropriate. As discussed above, Rule 302(b) of Regulation Crowdfunding requires an intermediary to provide to investors certain educational materials in connection with the opening of an account. In addition, proposed Rule 303(b)(2) of Regulation Crowdfunding would require an intermediary, each time before accepting an investment commitment, to obtain from the investor a representation that the investor has reviewed the intermediary's educational materials, understands that the entire amount of his or her investment may be lost and is in a financial condition to bear the loss of the investment.[799] The proposed rule would also require that an intermediary obtain from the investor answers to questions demonstrating the investor's understanding that there are restrictions on the investor's ability to cancel an investment commitment and obtain a return of his or her investment, that it

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[798] *See* Section II. Further, we anticipate that, because of the electronic nature of crowdfunding, many of the books and records maintained by intermediaries will be in electronic format. We expect this will enable the Commission to analyze data across the crowdfunding industry as part of its ongoing oversight. We note that Commission staff also expects to review the books and records practices of intermediaries as part of its planned three-year review.

[799] *See* Section II.C.4.b. (discussing Rule 302(b)(2) of Regulation Crowdfunding).

may be difficult for the investor to resell the securities, and that the investor should not invest any funds in a crowdfunding offering unless he or she can afford to lose the entire amount of his or her investment.

(b) Comments on the Proposed Rule

Several commenters supported the requirement that intermediaries obtain investor acknowledgments.[800] Some of these commenters, however, opposed requiring investors to re-acknowledge or to re-certify for each investment commitment.[801]

One commenter stated that investors should be required to complete and sign "subscription forms" that set forth, in addition to what the proposed rules would require, additional information concerning the investor's level of investment experience, the identity of any person from whom the investor acquired any information about the investment and the percentage of the investor's liquid net worth represented by the proposed investment.[802]

One commenter supported the Commission providing recommended forms of questions and representations, noting that "any material examples provided by the Commission will be helpful to both the investor and the intermediary."[803] However, another commenter stated that it would be opposed to the Commission providing recommended forms of questions as a "starting point" because such recommended forms could be seen as a safe harbor and constrain

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800 *See*, *e.g.*, Arctic Island Letter 6; CFA Institute Letter; Greenfield Letter; Joinvestor Letter; RocketHub Letter; STA Letter; Wefunder Letter.

801 *See* Wefunder Letter; RocketHub Letter (suggesting that once an account has been created on an intermediary platform, an investor should be able to invest in multiple offerings on the same intermediary platform without having to re-certify and review the educational materials).

802 *See* Greenfield Letter. *See also* STA Letter (stating that investors should be required to acknowledge that they are aware that "they may need to be diligent in notifying the issuer, or its designee, of any changes that would affect their ability to receive communications from the issuer"). We note, however, that issuers are not obligated to contact investors directly.

803 *See* Joinvestor Letter.

effectiveness.[804] In contrast, a different commenter stated that Commission-provided questions and representations should serve as a safe harbor so there is an incentive for issuers to use them.[805]

(c) Final Rules

After considering the comments, we are adopting Rule 302(b)(2) as proposed. As noted in the Proposing Release, this rule is intended to help ensure that investors engaging in transactions made in reliance on Section 4(a)(6) are fully informed and reminded of the risks associated with their particular investment before making any investment commitment. While an intermediary cannot ensure that all investors understand the risks involved, the rule requires intermediaries to confirm that an investor: (1) has reviewed the intermediary's educational materials delivered pursuant to Rule 302(b); (2) understands that the entire amount of his or her investment may be lost, and is in a financial condition to bear the loss of the investment; and (3) has completed a questionnaire demonstrating an understanding of the risks of any potential investment and other required statutory elements. In addition, the questionnaire required under the rule may help to address, at least in part, the concerns expressed by some commenters that Section 4A(a)(4) requires more than a mere self-certification.[806] We note, however, that the plain language of Section 4A(a)(4)(B) seemingly requires only that the investor positively affirms his or her understanding of the risk of loss.

Our final rule does not provide a model form of acknowledgment or questionnaire. Rather, the rule permits an intermediary to develop the representation and questionnaire in any format that is reasonably designed to demonstrate the investor's receipt of the information and

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804 *See* Wefunder Letter.

805 *See* Public Startup Letter 3.

806 *See, e.g.*, Accredify Letter; Commonwealth of Massachusetts Letter; Farnkoff Letter; Saunders Letter; Verinvest Letter.

compliance with the other requirements under the final rules. As with the educational material requirements, we continue to believe that rather than providing sample content or a model form of acknowledgment or questionnaire, intermediaries should be provided with sufficient flexibility to choose both the content, within the requirements of Rule 302(b), and the format used to present the required materials. Likewise, we also believe that an intermediary's familiarity with its business and likely investor base make it best able to determine the format in which to present the required materials. We note that any format used must be reasonably designed to demonstrate receipt and understanding of the information. There are many ways, especially on a web-based system, to convey information to, and obtain effective acknowledgment from, investors. As explained in the Proposing Release, the requirements of the rule would not be satisfied if, for example, an intermediary were to pre-select answers for an investor.

Further, an intermediary in its discretion may require additional information, such as information concerning the investor's level of investment experience, the identity of any person from whom the investor acquired any information about the investment and the percentage of the investor's liquid net worth represented by the proposed investment, or impose additional requirements on prospective investors, such as imposing express acknowledgments of the investor's responsibilities with respect to compliance.

Finally, although several commenters suggested that once an account has been created on an intermediary's platform, an investor should be able to invest in multiple offerings on the same intermediary platform without having to re-certify and review the educational material, we continue to believe that, in order to realize the statute's investor protection goals, it is prudent to require an intermediary to obtain an investor representation and completed questionnaire each time an investor seeks to make an investment commitment. Accordingly, under Rule 303(b), an

intermediary will be required to obtain these items each time an investor seeks to make an investment commitment.

c. Communication Channels

(1) Proposed Rule

Proposed Rule 303(c) of Regulation Crowdfunding would require an intermediary to provide, on its platform, channels through which investors can communicate with one another and with representatives of the issuer about offerings made available on the intermediary's platform. An intermediary that is a funding portal would be prohibited from participating in communications in these channels.[807] Proposed Rule 303(c) also would require the intermediary to: (1) make the communications channels publicly available; (2) permit only those persons who have opened accounts to post comments; and (3) require any person posting a comment in the communication channels to disclose whether he or she is a founder or an employee of an issuer engaging in promotional activities on behalf of the issuer, or is otherwise compensated, whether in the past or prospectively, to promote the issuer's offering.

(2) Comments on the Proposed Rule

We received comments both supporting[808] and opposing the proposed rules on communications channels.[809] Several commenters agreed that posting in communication channels should be limited to registered investors on an intermediary's platform.[810]

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807 *See* Rule 303(c)(1) (an intermediary that is a funding portal cannot "participate in these communications, other than to establish guidelines for communication and remove abusive or potentially fraudulent communications"). *See also* Exchange Act Section 3(a)(80) (defining the term "funding portal" as any person acting as an intermediary in a transaction involving the offer or sale of securities for the account of others, solely pursuant to Securities Act Section 4(a)(6), that does not, among other things, "offer investment advice or recommendations").

808 *See*, *e.g.*, PeoplePowerFund Letter; RocketHub Letter; Vann Letter (stating that intermediaries should be allowed to decide who may post on the channels).

Some commenters stated there should be more privacy or control in the manner in which comments are posted to the communications channels, such as submitting comments to intermediaries to review prior to posting or restricting the publicly viewable comments.[811] One commenter stated that he interprets the proposed rule to permit issuers to post videos and other promotional content (similar to marketing content used on non-securities-based crowdfunding sites like Kickstarter), and that he supported this approach as it would permit the issuer to "communicate freely and creatively . . . while giving the crowd a forum to ask questions or offer criticism."[812] Another commenter encouraged the Commission "to provide an investor 'hotline', where investors can report concerns relating to crowdfunding communications or transactions, and that intermediaries be required to provide notice on their platforms of how to access this hotline."[813]

Several commenters generally supported the disclosure requirement on communications by issuers or intermediaries and agreed that these communications should be made transparent to investors.[814]

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809 *See*, *e.g.*, Cromwell Letter (claiming that "[a]s [a] venture investor, you cannot judge the abilities of the management team over the Internet. Real venture capitalists do not make their investments over the Internet -- they spend hours and hours interviewing the founders / management team, in person. Small investors cannot successfully invest over the Internet, either."); Public Startup Letter 3; Moskowitz Letter (stating that the proposed rules do not prevent an accredited investor from, for example, posting a solicitation within the communication channels for more securities than he or she could purchase in the offering within his or her investment limits).

810 *See*, *e.g.*, PeoplePowerFund Letter; RocketHub Letter; Wefunder Letter.

811 *See*, *e.g.*, ASSOB Letter (stating that "random unmoderated comments" in communication channels should not be permitted, because it would allow for unacceptable solicitations or claims of return on investment); RocketHub Letter (expressing concern that certain confidential information may be disclosed between registered investors and the issuer, which would not be suitable for a public forum).

812 *See* Odhner Letter.

813 *See* CFA Institute Letter.

814 *See*, *e.g.*, CFA Institute Letter; RocketHub Letter (suggesting that intermediaries should be able to assist posters in disclosing their relationship to issuer).

One commenter generally supported the proposed rule requiring each promotional communication to be accompanied by disclosure of the receipt of past or prospective compensation.[815] Another commenter suggested that the proposed rules should be amended to require that intermediaries prominently post the online identities of the issuer's paid promoters in the communication channels.[816] One commenter, however, stated that the Commission should not mandate the exact methods by which an intermediary achieves compliance with the requirement for promoters to disclose their relationship with an issuer.[817]

In response to our request for comments, several commenters supported requiring intermediaries to keep the communication channels available to investors post-offering.[818] Another commenter, however, stated that the communication channels should be closed after stock certificates are issued and received by investors.[819] This commenter further noted that the continued maintenance of a communication channel after the end of a campaign would be an unnecessary cost. The same commenter suggested that the issuer's website is a better place for communication between investors and issuers.[820]

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815 *See* CFA Institute Letter.

816 *See* MCS Letter.

817 *See* Wefunder Letter (suggesting that the disclosures at the account opening stage are better devoted to the discussion of the risk of startup investing).

818 *See*, *e.g.*, PeoplePowerFund Letter (suggesting that the posting forum should be live and accessible to all website members not less than 30 days after the issue has been completed); RocketHub Letter; StartupValley Letter (suggesting that intermediaries should open a private channel of communication between investors and issuers for the post offering period and not use the same public channel that was used for the pre-offering and funding periods).

819 *See* RFPIA Letter.

820 *Id*. *See also* CfPA Letter (stating that ongoing communication between issuers and investors should be an obligation of issuers alone).

(3) Final Rule

After considering the comments, we are adopting Rule 303(c) as proposed. We considered commenters' suggestions that the issuer's website is a better place for communication between investors and issuers and that ongoing communication between issuers and investors should be an obligation of issuers alone. We believe, however, that communication channels on the intermediary's platform will provide a centralized and transparent means for members of the public that have opened an account with an intermediary to share their views about investment opportunities and to communicate with representatives of the issuer to better assess the issuer and investment opportunity.[821] While the JOBS Act does not impose this requirement, we believe it is consistent with the legislative intent that such a mechanism be in place for offerings made in reliance on Section 4(a)(6).[822] Also, though communications among investors may occur outside of the intermediary's platform, communications by an investor with a crowdfunding issuer or its representatives about the terms of the offering are required to occur through these channels[823] on the single platform through which the offering is conducted.[824] This requirement is expected to provide transparency and accountability, and thereby further the protection of investors.

Although one commenter stated that it interpreted the proposed rule to permit issuers to post videos and other promotional content, aside from Rule 303(c)(4) and its requirements for promotional activity, Rule 303(c) itself does not address the content or form used by issuers when

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821 *See also* discussion in Section II.B.5.

822 *See* 158 CONG. REC. S2231 (daily ed. Mar. 29, 2012) (statement of Sen. Scott Brown) ("In addition to facilitating communication between issuers and investors, intermediaries should allow fellow investors to endorse or provide feedback about issuers and offerings, provided that these investors are not employees of the intermediary. Investors' credentials should be included with their comments to aid the collective wisdom of the crowd.").

823 *See* Rule 204 of Regulation Crowdfunding and discussion in Section II.B.4.

824 *See* Rule 100(a)(3) of Regulation Crowdfunding and discussion in Section II.A.3.

communicating with investors through the channels provided on an intermediary's platform. Rather, Rule 204 of Regulation Crowdfunding sets forth the advertising requirements for issuers and, as explained above, Rule 204 allows an issuer to communicate with investors about the terms of the offering through communication channels provided by the intermediary on the intermediary's platform, so long as the issuer identifies itself as the issuer in all communications.[825]

We are requiring intermediaries to make the communications on the channels publicly available for viewing. We believe that this requirement is consistent with the concept of crowdfunding, as it provides for transparent crowd discussions about a potential investment opportunity. We also are requiring in Rule 303(c)(3) that intermediaries limit the posting in communication channels to those individuals who have opened an account with the intermediary on its platform. As stated in the Proposing Release, while we recognize that this requirement could narrow the range of views represented by excluding posts by anyone who has not opened an account with the intermediary, we believe that it will help to establish accountability for comments made in the communication channels. We continue to believe that, without this measure, there would be greater risk of the communications including unfounded, potentially abusive or biased statements intended to promote or discredit the issuer and improperly influence the investment decisions of members of the crowd.

With respect to one commenter's suggestion that the Commission provide an investor "hotline" where investors can report concerns relating to crowdfunding communications or transactions, we note that the Commission has an existing "Tips, Complaints and Referrals Portal"

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825 *See* Section II.B.4 (discussing Rule 204).

available on its website,[826] where the public may provide the Commission with information about potential fraud or wrongdoing involving alleged violations of the securities laws.

We are mindful of the cost associated with the communications channel, and, therefore, we are not requiring that intermediaries keep the communication channels available to investors post-offering, as suggested by some commenters.[827] However, an intermediary in its discretion can choose to maintain the communication channels post-offering.[828]

Consistent with the prohibition on a funding portal offering investment advice or recommendations,[829] the rule as adopted will prohibit an intermediary that is a funding portal from participating in any communications in these channels, apart from establishing guidelines for communication and removing abusive or potentially fraudulent communications. A funding portal can, for example, establish guidelines pertaining to the length or size of individual postings in the communication channels and can remove postings that include offensive or incendiary language. Also, although we understand the reasons for commenters' suggestions that there should be more privacy or control in the manner in which comments are posted, we believe that aside from intermediaries removing abusive or potentially fraudulent communications, investor protection is better served by providing the opportunity for uncensored and transparent crowd discussions about a potential investment opportunity.

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826 *See* Enforcement Tips and Complaints, *available at* https://www.sec.gov/complaint/tipscomplaint.shtml.

827 *See, e.g.*, PeoplePowerFund Letter; RocketHub Letter; StartupValley Letter.

828 It is important to note that an intermediary would still have to maintain records of such communications to satisfy the books and records requirements of the crowdfunding rules. *See* Rule 404(a)(3).

829 *See* Rule 300(c)(2)(i). Exchange Act Section 3(a)(80) defines the term "funding portal" as any person acting as an intermediary in a transaction involving the offer or sale of securities for the account of others, solely pursuant to Securities Act Section 4(a)(6), that does not, among other things, "offer investment advice or recommendations."

Finally, under the rule as adopted an intermediary must require any person posting on the communication channel to clearly and prominently disclose with each posting whether he or she is a founder or an employee of an issuer engaging in promotional activities on behalf of the issuer, or is otherwise compensated, whether in the past or prospectively, to promote the issuer's offering. This disclosure will apply to officers, directors and other representatives of the issuer, and also will be required of an intermediary that is a broker and its associated persons. We continue to believe that intermediaries, as the hosts of the communication channels, are well placed to take measures to ensure that promoters clearly identify themselves in their communication channels, in accordance with Securities Act Section 4A(b)(3).

d. Notice of Investment Commitment

(1) Proposed Rule

Proposed Rule 303(d) of Regulation Crowdfunding would require an intermediary, upon receipt of an investment commitment from an investor, to promptly give or send to the investor a notification disclosing: (1) the dollar amount of the investment commitment; (2) the price of the securities, if known; (3) the name of the issuer; and (4) the date and time by which the investor may cancel the investment commitment. Pursuant to proposed Rule 302(a)(2) of Regulation Crowdfunding, this notification would be provided by e-mail or other electronic media, and would be documented in accordance with applicable recordkeeping rules.[830]

[830] *See* Section II.C.4 (discussing Rule 100(a)(3)) and Section II.D.5 (discussing the recordkeeping rules applicable to funding portals). *See also* note 1114 (discussing the recordkeeping rules applicable to brokers and intermediaries).

(2) Comments on the Proposed Rule

Commenters generally supported the requirement that intermediaries send these notifications to investors.[831] One of these commenters stated that, in its view, the notice should be submitted twice: first, when an investor has made a commitment, and again when the cancellation period is over.[832] One commenter stated that, in its view, investors also should be notified of whether a campaign has been successful or not, both when the campaign is near completion and when the campaign has been closed.[833] However, one commenter opposed all notice requirements.[834]

(3) Final Rules

After considering the comments, we are adopting Rule 303(d) as proposed. As stated in the Proposing Release, the notification is intended, among other things, to provide the investor with a written record of the basic terms of the transaction, as well as a reminder of his or her ability to cancel the investment commitment. We believe that the adopted notification requirements will be useful to investors and provide transparency. We also believe that requiring that this notification be sent once—promptly upon receipt of an investment commitment from an investor—rather than multiple times as commenters suggested—will help to minimize the costs associated with providing additional notification, while still providing the investor with, among other things, an important reminder about the ability to cancel the investment commitment. Although an intermediary can decide, in its discretion, to provide additional notifications to its customers as a

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831 *See, e.g.*, CFA Institute Letter; Joinvestor Letter; RocketHub Letter.

832 *See* RocketHub Letter.

833 *See* Joinvestor Letter.

834 *See* Public Startup Letter 3.

business decision, we believe at this time that adopting additional notification requirements could hamper flexibility in the evolving crowdfunding market and potentially impair the development of best practices that are tailored to this unique form of raising capital.

e. Maintenance and Transmission of Funds

(1) Proposed Rule

Securities Act Section 4A(a)(7) requires that an intermediary "ensure that all offering proceeds are only provided to the issuer when the aggregate capital raised from all investors is equal to or greater than a target offering amount, . . . as the Commission shall, by rule, determine appropriate." Proposed Rule 303(e)(1) of Regulation Crowdfunding would implement this provision and address the maintenance and protection of investor funds, pending completion of a transaction made in reliance on Section 4(a)(6), by requiring an intermediary that is a registered broker to comply with established requirements in Exchange Act Rule 15c2-4[835] for the maintenance and transmission of investor funds.

Proposed Rule 303(e)(2) would establish separate requirements for an intermediary that is a funding portal. Because a funding portal cannot receive any funds, it would be required to direct investors to transmit money or other consideration directly to a "qualified third party" that has agreed in writing to hold the funds for the benefit of the investors and the issuer and to promptly transmit or return the funds to the persons entitled to such funds. Proposed Rule 303(e)(2) would define "qualified third party" to mean a bank[836] that has agreed in writing to either: (i) hold the funds in escrow for the persons who have the beneficial interests in the funds and to transmit or return the funds directly to the persons entitled to them when the appropriate event or contingency

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835 17 CFR 240.15c2-4.

836 *See* Exchange Act Section 3(a)(6) [15 U.S.C. 78c(a)(6)] (defining "bank").

has occurred; or (ii) establish a bank account (or accounts) for the exclusive benefit of investors and the issuer.

Proposed Rule 303(e)(3) would require an intermediary that is a funding portal to promptly direct transmission of funds from the qualified third party to the issuer when the aggregate amount of investment commitments from all investors is equal to or greater than the target amount of the offering and the cancellation period for each investor has expired, provided that in no event may the funding portal direct this transmission of funds earlier than 21 days after the date on which the intermediary makes publicly available on its platform the information required to be provided by the issuer under Rules 201 and 203(a) of proposed Regulation Crowdfunding.

(2) Comments on the Proposed Rule

Several commenters generally supported the proposed fund maintenance and transmission requirements.[837] One commenter suggested that intermediaries be allowed to reject an investor's investment commitment if that investor does not have a correlating balance in an account with the intermediary.[838] Another commenter suggested that the Commission require that such accounts be interest bearing and that either (1) the investors' funds be returned to them with their pro rata portion of the interest in the event the offering is canceled, or (2) the funds and the accrued interest be dispersed to the issuer upon the offering's successful closing.[839] Another commenter suggested that qualified third parties should be registered and verified for "reputations [of]

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[837] *See, e.g.*, Arctic Island Letter 6; ASTTC Letter; CSTTC Letter; Greenfield Letter (suggesting that the issuer should be required to certify in writing under penalty of perjury to the escrow bank that the offering has been completed pursuant to the terms in the offering statement and that there have been no material changes of circumstances that would render the representations in the offering statement false or misleading); Joinvestor Letter; STA Letter.

[838] *See* Zhang Letter.

[839] *See* MCS Letter.

integrity"; complaints against those entities should be made public; and "drawdown" schedules should be submitted at the onset of projects and subsequently control issuer access to "project funds."[840]

In the Proposing Release, we requested comment on various alternatives to the proposed rules. As to whether the proposed rules should prohibit any variations of a contingency offering, such as minimum-maximum, offerings, one commenter stated that the target amount of a crowdfunding campaign "should represent the minimum to avoid investor confusion" and that "oversubscription should be allowed."[841] This commenter noted that these conditions would allow companies to "choose to set their own minimum and maximum range."[842] Another commenter suggested that we permit contingency offers based on a maximum amount of funds being raised or other benchmarks if the maximum is not met or, alternatively, permit "all-or-none" offerings.[843]

As to whether other types of custody arrangements should be permitted, one commenter requested clarification that a carrying broker would not be deemed to accept any part of the sale price of any security for purposes of Exchange Act Rule 15c2-4 under specific circumstances.[844]

As to whether there should be a fixed deadline for transmission of funds (such as three business days), one commenter stated that "fixed deadlines should be set to protect investor and

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840 *See* Otherworld Letter.

841 *See* Joinvestor Letter.

842 *Id.*

843 *See* PeoplePowerFund Letter (suggesting also that any oversubscribed issues be allocated on a "first come first served" basis in connection with "all-or-none" offerings).

844 *See* FOLIOfn Letter. Although this commenter stated its belief that the proposed procedure is consistent with Rule 15c2-4 on the basis that the carrying broker would not be "accept[ing] any part of the sale price" until closing, at which time funds would be promptly transferred to the issuer, it stated that additional clarity would be helpful to ensure that the Proposing Release does not introduce confusion if read by some as containing an implication to the contrary.

issuer interests." This commenter suggested that "one week (7 days) should be sufficient to disburse collected funds."[845] Another commenter suggested a three-day deadline.[846]

As to whether SRO and staff guidance on Exchange Act Rule 15c2-4 should be expressly incorporated into the rules, one commenter suggested that there was no need for incorporation of prior guidance about Rule 15c2-4 into the proposed rules.[847]

As to whether the definition of "qualified third party" should be expanded to include entities other than a bank, one commenter stated that the Commission should "consider [permitting] non-bank custodians, such as internet services that specialize in escrow and payment transfer."[848] Another commenter suggested that "qualified third parties" should include credit unions, savings and loans and other institutions that offer similar protections to banks.[849] Similarly, another commenter suggested that credit unions should be included.[850] One commenter suggested that banks should not be a qualified third party.[851] One commenter suggested that the definition of "qualified third party" be expanded to include certain broker-dealers that "hold funds and securities on behalf of customer accounts pursuant to [Exchange Act] Rule 15c3-3 and

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845 *See* Joinvestor Letter.

846 *See* Public Startup Letter 3.

847 *See* Arctic Island Letter 6.

848 *See* Joinvestor Letter.

849 *See* Growthfountain Letter.

850 *See* Vann Letter.

851 *See* Public Startup Letter 3 (claiming that "[b]anks are unable to serve as the 'qualified third party'" and that no entities other than registered broker-dealers should serve this function in connection with Regulation Crowdfunding sales.). *But see* Computershare Letter (supporting the "inclusion of a requirement that Funding Portals use a qualified third party, which is a bank, to hold investor funds as escrow agent and transmit the funds to the issuer once the offering requirements are met"); ASTTC Letter (stating that it "strongly supports the Proposed Rule's requirement that Funding Portals be required to utilize qualified escrow agents to hold the investor assets prior to transmittal to issuers and that "[q]ualified escrow agents are generally regulated banks"); STA Letter (stating that "[it] is pleased that the Proposed Rules contain a requirement that Funding Portals transmit investor assets to qualified escrow agents, which are banks, prior to their release to the issuer.").

maintain net capital pursuant to [Exchange Act] Rule 15c3-1(a)(2)(i)".[852] The commenter also suggested that funding portals and other brokers should be able to utilize these brokers "to the identical degree they would be able to utilize banks under Rule 15c2-4."[853]

Commenters generally agreed with our proposed approach not to require funding portals to maintain net capital, noting among other things that imposing "net capital requirements would increase the cost of starting a new funding portal and reduce the potential number of intermediaries, while providing little additional protection to investors and issuers."[854]

As to whether certain methods of payment for the purchase of securities should either be required or prohibited, one commenter suggested that the types of payment methods not be limited in any way.[855] However, some commenters stated, generally, that credit cards should be prohibited as a form of payment for securities in connection with crowdfunding.[856]

(3) Final Rule

After considering the comments, we are adopting Rule 303(e) substantially as proposed, but with certain revisions in response to comments. Rule 303(e)(1), as adopted, requires an

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852 *See* FOLIOfn Letter. *See also* Arctic Island Letter 8 (suggesting that the rules permit a $250,000 net capital broker-dealer to act as trustee for an omnibus escrow account at an FDIC insured bank); Ex 24 Letter.

853 *See* FOLIOfn Letter (stating also its belief that the brokers "should be distinguished from other broker-dealers in the context of Regulation Crowdfunding and not be subject to the requirements of SEC Rule 15c2-4(b)").

854 *See* Tiny Cat Letter (stating that "[f]unding portals are already prohibited from handling funds and securities, and are also subject to a fidelity bond in the proposed regulations"). *See also* Joinvestor Letter (suggesting that since funding portals will not be monetary custodians, there should be no net capital requirement instituted); Vann Letter (stating that a "capital requirement would unnecessarily restrict competition").

855 *See* Public Startup Letter 3.

856 *See, e.g.*, Arctic Island Letter 6 (suggesting that, given the chargeback periods for credit cards, broker-dealers should only be permitted to accept credit card payments from investors if the broker-dealer "directly and unconditionally guarantees the amounts obtained thereby to both the issuer and the escrow agent"); Consumer Federation Letter (suggesting that allowing payment via credit card increases the risk that investors will make crowdfunding investments that they cannot afford); Joinvestor Letter; RocketHub Letter (stating that "[p]ermitting debt-based payment vehicles, such as credit cards, which have their own rescission policies, (i.e., charge backs) is problematic").

intermediary that is a registered broker-dealer to comply with established requirements in Exchange Act Rule 15c2-4 for the maintenance and transmission of investor funds. Rule 15c2-4 requires, in relevant part, that in connection with a contingency offering of a security, any money or other consideration received by a broker-dealer participating in the distribution must be promptly deposited in a separate bank account, as agent or trustee for the persons who have the beneficial interest therein, until the appropriate event or contingency has occurred, and thereafter promptly transmitted or returned to the persons entitled thereto;[857] or alternatively, that all such funds must be promptly transmitted to a bank that has agreed in writing to hold such funds in escrow for the persons who have the beneficial interests therein and to transmit or return such funds directly to the persons entitled thereto when the appropriate event or contingency has occurred.[858] When the Commission adopted Rule 15c2-4, the Commission explained that the rule was designed to prevent fraud by a broker-dealer "either upon the person on whose behalf the distribution is being made or upon the customer to whom the payment is to be returned if the distribution is not completed."[859] As such, consistent with Securities Act Section 4A(a)(7), the intermediary may transmit the proceeds to the issuer only if the target offering amount is met or exceeded.

Rule 303(e)(2) as adopted establishes separate requirements for an intermediary that is a funding portal (as compared to an intermediary that is a broker-dealer) because a funding portal

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857 *See* Exchange Act Rule 15c2-4(b)(1). We note, however, that any broker-dealer seeking to hold such investor funds in a separate bank account as agent or trustee for the persons who have a beneficial interest therein are still subject to net capital requirements pursuant to Exchange Act Rule 15c3-1.

858 *See* Exchange Act Rule 15c2-4(b)(2).

859 *Adoption of Rule 15c2-4 under the Securities Exchange Act of 1934*, Release No. 34-6737 (Feb. 21, 1962) [27 F.R. 2089 (Mar. 3, 1962)].

cannot, by statute, hold, manage, possess, or otherwise handle investor funds or securities.[860] Therefore, Rule 303(e)(2) requires a funding portal to direct investors to transmit money or other consideration directly to a qualified third party that has agreed in writing[861] to hold the funds for the benefit of the investors and the issuer and to promptly transmit or return the funds to the persons entitled to such funds.[862]

We are revising the definition of a "qualified third party" to include for purposes of the final rule: a registered broker or dealer that carries customer or broker or dealer accounts and holds funds or securities for those persons,[863] a bank, or a credit union insured by the National Credit Union Administration ("NCUA").[864] We had proposed to define "qualified third party" to mean a bank[865] because investors, as well as intermediaries and issuers, would then be afforded the protections of existing regulations that apply to banks, in particular those pertaining to the

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860 *See* Exchange Act Section 3(a)(80)(D).

861 This written agreement is required to be maintained by the funding portal pursuant to proposed Rule 404 of Regulation Crowdfunding. *See* Section II.D.5.

862 In the crowdfunding context, we expect that the intermediary will make the determination as to whether the contingency (*i.e.*, the target offering amount) has been met. *See* Securities Act Section 4A(a)(7) (requiring that an intermediary "ensure that all offering proceeds are only provided to the issuer when the aggregate capital raised from all investors is equal to or greater than a target offering amount, . . . as the Commission shall, by rule, determine appropriate.").

863 Broker-dealers that may serve as qualified third parties under Rule 303(e) include only those broker-dealers that are required to maintain minimum net capital of $250,000 or a higher minimum amount depending on their status under Appendix E of Rule 15c3-1 under the Exchange Act. *See* Exchange Act Rules 15c3-1(a)(2)(i) and 15c3-1(a)(7)(i).

864 The NCUA was established by the Federal Credit Union Act of 1934. *See* Federal Credit Union Act of 1934, as amended, 12 U.S.C. 1752 *et seq.* The NCUA administers the National Credit Union Share Insurance Fund ("NCUSIF"), which is backed by the full faith and credit of the U.S. government. NCUSIF protection covers the deposits in federal credit unions, as well as a majority of state-chartered credit unions. *See* NCUA Share Insurance Fund Information, Reports, and Statements, Frequently Asked Questions, NATIONAL CREDIT UNION ADMINISTRATION, http://www.ncua.gov/DataApps/Pages/SI-FAQs.aspx.

865 *See* Proposing Release, at 182-83 [78 FR 66427, at 66473]. *See also* Exchange Act Section 3(a)(6) [15 U.S.C. 78c(a)(6)] (defining "bank").

safeguarding of customer funds.[866] However, after considering the comments, we agree with those commenters who suggested that the definition of "qualified third party" should be expanded to include entities other than a bank and should include, as one commenter suggested, credit unions provided that these entities offer similar protections to banks.[867] We also made a corresponding change to the language of the rule text to indicate that a qualified third party arrangement may involve either a bank or credit union account (or accounts) established for the exclusive benefit of investors and the issuer.

After considering the comments, we further believe that the definition of "qualified third party" should be expanded to include certain types of registered broker-dealers. We are expanding the definition to include registered broker-dealers that carry customer or broker or dealer accounts and holds funds or securities for those persons. We believe such brokers-dealers are appropriate entities to serve as qualified third parties as they are subject to various regulatory obligations, which are designed to provide enhanced protection of investor funds through the imposition of capital and other requirements.[868] We note that we are not amending the requirements of Rule 15c2-4 through this release and not distinguishing broker-dealers that participate in offerings made in reliance on Securities Act Section 4(a)(6), either as a qualified

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866 For example, bank deposit accounts at FDIC-insured banks are protected by FDIC deposit insurance. *See* Federal Deposit Insurance Corp., Deposit Insurance FAQs, *available at* http://www.fdic.gov/deposit/deposits/faq.html.

867 We do not believe that the definition of qualified third party should be extended to include Internet service providers that specialize in escrow and payment transfer, as suggested by one commenter, because we do not believe that such entities are governed by a regulatory scheme designed to provide similar protections as the other entities that we are defining as qualified third parties under Rule 303(e). We note that another commenter suggested the addition of savings and loan associations. We believe that certain savings and loan associations are covered by the definition of "bank" under Exchange Act Section 3(a)(6), and as such, are qualified third parties under Rule 303(e). We note that the Federal Deposit Insurance Corp. extended its authority to cover savings and loan associations in 1989. *See* Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA) (creating the Savings Association Insurance Fund (SAIF)).

868 *See, e.g.*, Exchange Act Rule 15c3-1 and Rule 15c2-4.

third party or an intermediary, from broker-dealers in any other contingency offerings. As such, broker-dealers participating in offerings made in reliance on Section 4(a)(6), either as an intermediary or as a qualified third party, are still subject to Rule 15c2-4.[869] Further, we believe that existing Commission and staff guidance on Rule 15c2-4 is extensive and clear and does not warrant incorporation into the final rule or clarification.

The statute does not limit or require a particular payment mechanism, and we are not imposing such a restriction because we believe that the rules should provide reasonable flexibility regarding the payment mechanisms intermediaries employ. We believe that restrictions on particular payment mechanisms would not serve to significantly increase investor protection, particularly in light of the established investment limits. We note, however that an intermediary can, in its discretion, decline to accept certain payment methods, such as credit cards, or accept them only in certain circumstances.[870]

We also are not adopting additional requirements that would, for example, (1) prohibit variations of a contingency offering, such as minimum-maximum offerings; (2) establish a fixed deadline for transmission of funds as compared to the proposed requirement to transmit funds "promptly"; or (3) require funding portals to maintain a certain amount of net capital. We believe that additional restrictions, such as prohibiting variations of a contingency offering or establishing

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869 Under existing Rule 15c2-4, the qualified third party broker-dealer will be required to promptly deposit the funds in a separate bank account, as agent or trustee for the persons who have the beneficial interest therein, until the appropriate event or contingency has occurred, and thereafter promptly transmit or return the funds to the persons entitled thereto. *See* Rule 15c2-4(b)(1).

870 We note, for example, that an intermediary can, in its discretion, decline to accept credit cards given that, as at least one commenter suggested, an investor's use of his or her right to dispute credit card charges can inhibit the ability of an issuer to meet its target or to provide accurate disclosures to investors and the Commission regarding the progress it has made toward, and whether it has, reached the target offering amount. This potential impact will affect offerings conducted through brokers and funding portals alike. We also note that pursuant to Exchange Act Section 3(a)(80)(D) (15 U.S.C. 78c(a)(80)(D)), a funding portal is statutorily prohibited from extending credit or margin to customers.

a fixed deadline for the transmission of funds could hamper flexibility in the nascent crowdfunding market and prohibit the development of best practices specifically tailored to this unique form of capital raising. Finally, we are not requiring in the final rule net capital standards for funding portals. As noted above, funding portals are prohibited from handling, managing or possessing investor funds or securities.[871] We continue to believe that the requirements relating, in particular, to transmission of proceeds under the final rules will help ensure that investor funds are protected, without requiring funding portals to maintain net capital.

f. Confirmation of Transactions

(1) Proposed Rule

As proposed, Rule 303(f)(1) of Regulation Crowdfunding would require that an intermediary, at or before the completion of a transaction made pursuant to Section 4(a)(6), give or send to each investor a notification disclosing: (1) the date of the transaction; (2) the type of security that the investor is purchasing; (3) the identity, price and number of securities purchased by the investor, as well as the number of securities sold by the issuer in the transaction and the price(s) at which the securities were sold; (4) certain specified terms of the security, if it is a debt or callable security; and (5) the source and amount of any remuneration received or to be received by the intermediary in connection with the transaction, whether from the issuer or from other persons. This notification would be required to be provided by e-mail or other electronic media,[872] and to be documented in accordance with applicable recordkeeping rules.[873] Pursuant to

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871 *See* Exchange Act Section 3(a)(80)(D) [15 U.S.C. 78c(a)(80)(D)] and discussion in Section II.C.1.

872 *See* proposed Rule 302(a)(2) (requiring an intermediary to provide all information electronically). *See also* Section II.C.4.a (discussing electronic delivery requirements).

873 Intermediaries that are brokers are subject to the recordkeeping requirements of Exchange Act Rules 17a-3 and 17a-4, and intermediaries that are funding portals are subject to recordkeeping requirements under Rule

proposed Rule 303(f)(2), an intermediary that gives or sends to each investor the notification described above would be exempt from the requirements of Exchange Act Rule 10b-10[874] for the subject transaction.

(2) Comments on the Proposed Rule

Commenters generally supported the proposed confirmation requirements.[875] One commenter, however, stated its view that permitting intermediaries to satisfy the delivery requirement for transaction confirmations through delivery of a message that contains a notice that the information is available on the intermediary's website would not be sufficient.[876]

(3) Final Rule

After considering the comments, we are adopting Rule 303(f), as proposed, but with one clarifying change. As proposed, Rule 303(f)(1)(vi) would have required an intermediary to give or send to each investor a notification disclosing: "[t]he source and amount of any remuneration received or to be received by the intermediary in connection with the transaction, including the amount and form of any remuneration that is received, or will be received, by the intermediary from persons other than the issuer. We are revising Rule 303(f)(1)(vi) to require disclosure as well of the form of any remuneration received or to be received by the intermediary in connection with the transaction, including any remuneration received or to be received by the intermediary from persons other than the issuer. This edit is intended to clarify the rule by placing "source, form and amount" together, rather than having "form" listed out separately as proposed.

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404 of Regulation Crowdfunding. *See* note 1114 (discussing the recordkeeping rules applicable to brokers and intermediaries). *See also* Section II.D.5.

874 *See* note 882 (discussing Exchange Act Rule 10b-10 (17 CFR 240.10b-10) generally).

875 *See, e.g.*, CFA Institute Letter; Joinvestor Letter.

876 *See* Consumer Federation Letter (stating that "[w]hile most if not all intermediaries would be likely to deliver the actual confirmation to investors, the rule would not guarantee this").

As explained in the Proposing Release, we believe that transaction confirmations serve an important and basic investor protection function by, among other things, conveying information and providing a reference document that allows investors to verify the terms of their transactions, acting as a safeguard against fraud and providing investors a means by which to evaluate the costs of their transactions.[877] Each of the required items of information is intended to assist investors in memorializing and assessing their transactions. Furthermore, the requirement that an intermediary disclose to an investor the source, form and amount of any remuneration received or to be received is designed to help to highlight potential conflicts of interest if, for example, an intermediary has a financial interest in an issuer using its services. [878]

As for the concern raised by one commenter about the delivery requirements for transaction confirmations,[879] we note, as we did in the Proposing Release, that the confirmation is required to be provided by e-mail or other electronic media, consistent with the Commission's long-standing policies on the use of electronic media for delivery purposes.[880] This is also consistent with the requirement for an intermediary to provide all information electronically. We believe that this delivery requirement is appropriate for crowdfunding transactions and satisfies our obligation that requirements under Securities Act Section 4A(a)(12) be for the protection of

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877 *See* Proposing Release at 78 FR 66475. *See also Confirmation of Transactions*, Release No. 34-34962 (Nov. 10, 1994) [59 FR 59612, 59613 (Nov. 17, 1994)].

878 Although Securities Act Section 4A(a)(11) requires an intermediary to prohibit its directors, officers or partners (or any person occupying a similar status or performing a similar function) from having any financial interest in an issuer using its services, the final rules do not include a complete prohibition on the intermediary, itself, having a financial interest in an issuer using its services. The intermediary may have a financial interest in an issuer using its services, subject to certain limitations. *See* Rule 300(b). *See also* Section II.C.2.b.

879 *See* Consumer Federation Letter.

880 *See* Proposing Release, at 189 [78 FR 66427, at 66475]. *See also Use of Electronic Media*, note 714 at 25853 (discussing the "access equals delivery" concept and citing *Use of Electronic Media for Delivery Purposes*, Release No. 34-36345 (Oct. 6, 1995) [60 FR 53548, 53454 (Oct. 13, 1995)])).

investors and in the public interest. As to the same commenter's view that the rule would not guarantee delivery of a confirmation to investors,[881] although we acknowledge that statutes and rules cannot guarantee compliance, there is a robust regulatory scheme in place that is designed to promote compliance and that is coupled with supervision and enforcement by both the Commission and the registered national securities association.

In addition, under Rule 303(f)(2) as adopted, an intermediary that gives or sends to each investor the notification described above is exempt from the requirements of Exchange Act Rule 10b-10 for the subject transaction.[882] The confirmation terms under Rule 303(f)(2) are similar to, but not as extensive as, those broker-dealers are subject to under Rule 10b-10. We believe that this difference is appropriate given the more limited scope of an intermediary's role in crowdfunding transactions. Rule 10b–10, for example, requires disclosure about such matters as payment for order flow, riskless principal transactions, payment of odd-lot differentials and asset-backed securities. These items generally would not be relevant to crowdfunding securities transactions or an intermediary's participation in such transactions, and their inclusion in a

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881 *See* Consumer Federation Letter.

882 Exchange Act Rule 10b-10 (17 CFR 240.10b-10) generally requires a broker-dealer effecting a customer transaction in securities (other than U.S. savings bonds or municipal securities) to provide a notification to its customer, at or before completion of a securities transaction, that discloses certain information specific to the transaction. Specifically, Rule 10b-10 requires the disclosure of the date, time, identity, prices and number of securities bought or sold; the capacity in which the broker-dealer acted (*e.g.*, as agent or principal); yields on debt securities; and under specified circumstances, the amount of remuneration the broker-dealer will receive from the customer and any other parties. With regard to the specified circumstances mentioned above, the remuneration disclosures of Rule 10b-10 generally are required, but certain exclusions apply. For example, the remuneration disclosures are generally required where a broker or dealer is acting as agent for a customer or some other person. In the case where remuneration is received or to be received by the broker from such customer in connection with the transaction, the disclosures are not required where the remuneration paid by such customer is determined pursuant to written agreement with such customer, otherwise than on a transaction basis. 17 CFR 240.10b-10(a)(2)(i)(B). In contrast, the remuneration disclosure requirements of Rule 303(f)(2)(vi) are required across all crowdfunding transactions where remunerations are received or are to be received. Given the limits on the dollar amount of securities that can be offered, as well as the limits on individual investment amounts, in transactions relying on Section 4(a)(6), we do not expect investors to negotiate individualized compensation agreements.

crowdfunding securities confirmation may be confusing to investors. Therefore, we believe that if an intermediary satisfies the notification requirements of the final rules, the intermediary will have provided investors with sufficient relevant information about the crowdfunding security, and so should not be required to meet the additional requirements of Rule 10b–10.

6. Completion of Offerings, Cancellations and Reconfirmations

a. Proposed Rule

Under Securities Act Section 4A(a)(7), an intermediary is required to allow investors to cancel their commitments to invest as the Commission shall, by rule, determine appropriate. Securities Act Section 4A(b)(1)(G) requires an issuer, prior to sale, to provide investors "a reasonable opportunity to rescind the commitment to purchase the securities." We proposed, therefore, in Rule 304(a) of Regulation Crowdfunding, to give investors an unconditional right to cancel an investment commitment for any reason until 48 hours prior to the deadline identified in the issuer's offering materials. Under this approach, an investor could reconsider his or her investment decision with the benefit of the views of the crowd and other information, until the final 48 hours of the offering. Thereafter, an investor would not be able to cancel any investment commitments made within the final 48 hours of the offering (except in the event of a material change to the offering, as discussed below).[883]

We also proposed in Rule 304(b) that if an issuer reached the target offering amount prior to the deadline identified in its offering materials, it could close the offering once the target offering amount was reached, provided that: (1) the offering had been open for a minimum of 21 days; (2) the intermediary provided notice about the new offering deadline at least five business days prior to the new offering deadline; (3) investors would be given the opportunity to reconsider

[883] *See* proposed Rule 304(c).

their investment decision and to cancel their investment commitment until 48 hours prior to the new offering deadline; and (4) at the time of the new offering deadline, the issuer continued to meet or exceed the target offering amount.

In addition, we proposed in Rule 304(c) that if there was a material change[884] to the terms of an offering or to the information provided by the issuer about the offering, the intermediary would be required to give or send to any investors who have made investment commitments notice of the material change, stating that the investor's investment commitment will be cancelled unless the investor reconfirms his or her commitment within five business days of receipt of the notice.[885] As proposed, if the investor failed to reconfirm his or her investment within those five business days, the intermediary would be required, within five business days thereafter, to: (1) provide or send the investor a notification disclosing that the investment commitment was cancelled, the reason for the cancellation and the refund amount that the investor should expect to receive; and (2) direct the refund of investor funds.[886] This notification, like other notifications from an intermediary, would be required to be provided by e-mail or other electronic media, and to be documented in accordance with applicable recordkeeping rules.[887]

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884 In the Proposing Release, we noted that in those instances where an issuer had previously disclosed in its offering materials only the method for determining the price of the securities offered and not the final price of those securities, setting of the final price would be considered a material change. We also noted that if the change involved closing the offering once the target offering amount is reached, which would be prior to the deadline identified in the offering materials, then the procedures required under proposed Rule 304(b), and not those in Rule 304(c), would apply.

885 The proposed rules also required that an issuer extend an offering to allow for a five business day period in instances where material changes to the offering or to the information provided by the issuer occurred within five business days of the maximum number of days that an offering was to remain open. *See* proposed Rule 304(c)(2) of Regulation Crowdfunding. *See also* Rule 302(a)(2) (requiring that notification be provided by email or through other electronic media).

886 *See* proposed Rule 304(c)(1) of Regulation Crowdfunding.

887 Intermediaries that are brokers would be subject to the recordkeeping requirements of Exchange Act Rules 17a-3 and 17a-4, and intermediaries that are funding portals would be subject to recordkeeping requirements under proposed Rule 404 of Regulation Crowdfunding. *See* note 1114 (discussing the recordkeeping rules

Finally, we proposed in Rule 304(d) that if an issuer did not complete an offering, for example, because the target was not reached or the issuer decided to terminate the offering, the intermediary would be required, within five business days, to: (1) give or send to each investor who had made an investment commitment a notification disclosing the cancellation of the offering, the reason for the cancelation, and the refund amount that the investor should expect to receive; (2) direct the refund of investor funds; and (3) prevent investors from making investment commitments with respect to that offering on its platform. This notification, like other notifications from an intermediary, would be required to be provided by e-mail or other electronic media, and to be documented in accordance with applicable recordkeeping rules.[888]

b. Comments on the Proposed Rule

One commenter supported the unconditional right of investors to cancel an investment commitment for any reason until 48 hours prior to the close of an offering.[889] Other commenters, however, expressed concern over the potential for misconduct regarding cancellations,[890] such as scenarios where investors commit and then withdraw at the last minute.[891]

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applicable to brokers and intermediaries). *See also* Section II.D.5; Section II.C.4. (discussing an intermediary's electronic delivery requirements and Rule 302(a)(2)).

888 *See* note 1114 (discussing the recordkeeping rules applicable to brokers and intermediaries).

889 *See* CFA Institute Letter.

890 *See, e.g.,* Joinvestor Letter (suggesting the lock-in-date should be fourteen days prior to the closing date to prevent any misconduct surrounding the approach of a target, or the limit of oversubscription, near to the close of the round); Consumer Federation Letter; RocketHub Letter.

891 *See, e.g.,* RocketHub Letter (recommending a 24-hour cancellation period in order to protect investors from "'pump & rescind' schemes" and minimize an issuer's exposure to the risk of "'short fall' situations"); Consumer Federation Letter (noting the risk that "individuals associated with the issuer will commit money to the offering early in the process in order to stimulate interest and create a sense of urgency about investing, only to withdraw at the last minute"). The same commenter suggested that potential gamesmanship by investors associated with the issuer has the potential to discredit crowdfunding and recommended that the Commission consider more meaningful restrictions on issuer participation.

One commenter stated that the rule on early closure of an offering should be more narrowly defined.[892] This commenter requested that the Commission clarify whether, under such circumstances, an offering should be closed from accepting more funds or keep accepting commitments until the end of the five business day period, even if this puts an offering over set limits.[893]

Some commenters supported the proposal that existing disclosure materials can be modified in the event of a material change, with the original offering remaining open,[894] while one commenter also suggested that no changes should be allowed within 21 days of the close date.[895] Several commenters generally agreed that an investor should have to reconfirm the commitment to invest when a material change occurs.[896] One commenter stated that many investors would prefer not to have to re-confirm their investments and recommended allowing investors to decide how to handle material changes.[897] Another commenter opposed any reconfirmation requirement because it believed there should be a presumption that any changes made would be in the best interest of the issuer and all of its stakeholders.[898]

Some commenters supported the proposed five-day reconfirmation period for investors.[899] Some commenters, however, stated that five business days is not enough time for an investor to

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892 *See* RFPIA Letter (stating that "[i]f the issuer reaches the target offering amount prior to the deadline the current proposed regulation require[s] a funding portal to give a 5 day notice to investors of the new closing date. Since funding portals have no crystal balls, this process needs to be more narrowly defined").

893 *Id*.

894 *See, e.g.,* Arctic Island Letter 6; Joinvestor Letter; Wales Capital Letter 2.

895 *See* Joinvestor Letter.

896 *See, e.g.,* CFA Institute Letter; Wales Capital 2 Letter.

897 *See* Wefunder Letter.

898 *See* Public Startup Letter 3.

899 *See, e.g.,* CFA Institute Letter; Wales Capital 2 Letter.

decide whether to reconfirm an investment commitment after a material change is made by the issuer.[900] One commenter suggested a shorter reconfirmation time period.[901] Another commenter recommended that the Commission clarify when the five-day reconfirmation period begins.[902] One commenter suggested material revisions made to the offering should restart the 21-day minimum period for the campaign, though generally agreed that a five-business day notification is sufficient in the event that an offering is cancelled.[903]

c. Final Rules

We are adopting Rule 304 as proposed, with a technical change to correct a cross-cite in the rule text. We believe that the final rule appropriately takes into consideration the needs of investors to be able to consider material changes to the terms of the offering and new views expressed by the crowd, while allowing issuers to have certainty about their ability to close an offering at the end of the offering period. We have considered the comments outlined above about concerns with cancellation generally and those suggesting other types of cancellation or lock-in periods. However, we continue to believe that allowing investors to cancel any investment commitments for any reason until 48 hours prior to the deadline identified in the issuer's offering materials is an appropriate cancellation period because it is consistent with the requirement of Section 4A(b)(1)(G) that investors have a "reasonable opportunity" to rescind investment commitments, while also providing issuers with certainty within a reasonable amount of time

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900 *See, e.g.,* Arctic Island Letter 6 (advocating that the time period be "indefinite" so as to give investors more time to consider the changes and to give issuers more time to answer questions of individual investors and provide clarifications or make subsequent changes as needed); CfPA Letter (recommending that any change in offering documents on a website after initial posting restart the 21-day period (or at least half of that) during which offerings cannot close and prospective or pledged investors can reconsider and rescind their commitments).

901 *See* RFPIA Letter (suggesting eliminating the requirement or reducing it to 72 hours).

902 *See* ODS Letter.

903 *See* Wales Capital Letter 2.

about whether they have indeed received investment commitments. Although we acknowledge commenters' concerns about potential misconduct in connection with cancellations of investment commitments, we note that issuers and investors, including investors associated with the issuer, are subject to the antifraud provisions of the securities laws. We also note that, as we discussed above, an intermediary is required to promptly remove an offering from its platform if it becomes aware of information that causes it to believe that the issuer or the offering presents the potential for fraud or otherwise raises concerns about investor protection.[904]

In regards to one commenter's request for clarification as to whether an intermediary may continue to receive investment commitments during the five business day period prior to an early closure of an offering (even if the commitment may be oversubscribed), we note that intermediaries are permitted to continue to receive investment commitments during that time period, provided that the intermediary informs investors about the continuation of such acceptance in accordance with Rule 304(b).[905]

In addition, we believe that when material changes arise during the course of an offering, an investor who had made a prior investment commitment should have a reasonable period during which to review the new information and to decide whether to invest by reconfirming the investment commitment. Despite some commenters' concerns outlined above, we continue to believe that a five business day period is appropriate because it reasonably reflects the need to allow an investor sufficient time to consider material changes to the terms of the offering while

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904 *See* Section II.C.3.

905 However, the issuer will still have to comply with the rules regarding oversubscriptions. *See* Section II.B.6.a. This same commenter expressed uncertainty about how an issuer will communicate early closure to a funding portal so that the funding portal can provide appropriate notice to investors about the new offering deadline. The final rules do not prescribe the mechanics for how funding portals must communicate with issuers as we believe the better course is to provide for flexibility in this regard so that intermediaries and issuers can arrive at efficient working arrangements.

giving issuers certainty about their ability to close an offering. For the same reasons noted above, we also believe that five business days is a sufficient amount of time for intermediaries to notify investors about offerings that are not completed or terminated. Finally, we believe that requiring an investor to reconfirm his or her investment commitment within five business days of receipt of the notice of a material change is sufficiently clear as to when the reconfirmation period begins and provides additional investor protection and is therefore an appropriate requirement for the final rule.

7. Payments to Third Parties

a. Proposed Rule

Securities Act Section 4A(a)(10) provides that an intermediary in a transaction made in reliance on Section 4(a)(6) shall not compensate "promoters, finders, or lead generators for providing the broker or funding portal with the personal identifying information of any potential investor."

We proposed in Rule 305(a) of Regulation Crowdfunding to prohibit an intermediary from compensating any person for providing it with the "personally identifiable information"[906] of any investor. As explained in the Proposing Release, we believe that any person compensated for providing the personally identifiable information of investors would be acting as a promoter, finder or lead generator within the meaning of Securities Act Section 4A(a)(10).

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[906] As proposed, the term "personally identifiable information" would mean any information that can be used to distinguish or trace an individual's identity, either alone or when combined with other personal or identifying information that is linked or linkable to a specific individual. *See* proposed Rule 305(c) of Regulation Crowdfunding. As explained in the Proposing Release, personally identifiable information could include any information that can be used to identify an individual, such as name, social security number, date or place of birth, mother's maiden name or biometric records, as well as any other information that is linked directly to an individual, such as financial, employment, educational or medical information.

Proposed Rule 305(b), however, would permit an intermediary to compensate a person for directing issuers or investors to the intermediary's platform if: (1) the person does not provide the intermediary with the personally identifiable information of any investor, and (2) the compensation, unless it is paid to a registered broker or dealer, is not based, directly or indirectly, on the purchase or sale of a security offered in reliance on Securities Act Section 4(a)(6) on or through the intermediary's platform.[907]

b. Comments on the Proposed Rule

Some commenters generally supported the portion of the proposed rule that allows intermediaries to compensate third parties for directing investors to the platform.[908] Some of these comments also agreed that intermediaries should be permitted to compensate third parties for general business advertising including, for example, web search engine direction or other standard Internet marketing techniques.[909] In response to our request for comment as to whether disclosures should be required when an intermediary compensates third parties for directing investors to its platform, one commenter suggested the Commission should not require disclosure of "standard Internet marketing [practices]" that "inform investors of companies they may be interested in."[910] Another commenter stated that compensation should only be allowed under limited circumstances, albeit without providing examples of those limited circumstances.[911] We

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907 We note that the receipt of direct or indirect transaction-based compensation would strongly indicate that the recipient is acting as a broker. As such, the party receiving the compensation in the scenario described needs to consider whether it would be required to register as a broker.

908 *See, e.g.,* RoC Letter; RocketHub Letter; Wefunder Letter.

909 *See, e.g.,* RocketHub Letter; Wefunder Letter. *See also* ABA Letter (discussing the practice of so-called "passive bulletin boards").

910 Wefunder Letter.

911 *See* Joinvestor Letter ("We believe such compensation should be allowed under extremely limited circumstances, as promotion will be a central issue to these campaigns.").

did not receive comments related to the definition of the term "personally identifiable information" as proposed in Rule 305(c).

c. Final Rules

We are adopting Rule 305 with modifications. Rule 305(a), like the proposed rule, states that an intermediary may not compensate any person for providing the intermediary with the personally identifiable information of any investor in securities offered and sold in reliance on Section 4(a)(6) of the Securities Act. However, we are not including in the final rule what was proposed in paragraph (b), which stated that an intermediary may compensate a person for directing issuers to the intermediary's platform, provided that unless the compensation is made to a registered broker or dealer, the compensation is not based, directly or indirectly, on the purchase or sale of a security offered in reliance on Section 4(a)(6) of the Securities Act on or through the intermediary's platform. Upon further consideration, we believe this provision would be duplicative of Rule 402(b)(6), which addresses referral payments that funding portals are permitted to pay to third parties.[912] In addition, registered broker-dealers are already subject to limitations on the types of compensation that they may pay to third parties, and as we explained in the Proposing Release, are subject to an established regulatory and oversight regime that provides important safeguards for investors.

We agree with those commenters who believe intermediaries should be permitted to compensate third parties for general business advertising including, for example, web search engine direction or other standard Internet marketing techniques so long as that compensation is not based, directly or indirectly, on the purchase or sale of a security offered in reliance on

[912] *See* Section II.D.3.

Securities Act Section 4(a)(6).[913] We believe permitting compensation for these types of general business advertising does not raise the same privacy concerns as those implicated by the provision of personally identifiable information and is generally consistent with the statutory scheme for crowdfunding promotional activities. Therefore, under the rules, an intermediary may pay a person a flat fixed fee[914] to direct persons to the intermediary's platform through, for example, hyperlinks or search term results or make payments to a person to advertise its existence.[915] The intermediary, however, cannot pay to receive personally identifiable information in under any circumstances pursuant to the prohibition in Rule 305(a).

Finally, we are adopting as proposed the definition of personally identifiable information, which will be renumbered as Rule 305(b).

D. Additional Funding Portal Requirements

1. Registration Requirement

a. Generally

(1) Proposed Rules

Securities Act Section 4A(a)(1) requires that an intermediary facilitating a transaction made in reliance on Securities Act Section 4(a)(6) register with the Commission as a broker or a funding portal. The statute does not, however, prescribe the manner in which a funding portal

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913 *See, e.g.*, 158 Cong. Rec. S5474-03 (daily ed. July 26, 2012) (statement of Sen. Jeff Merkley) ("[T]he limitation on off-platform advertising is intended to prohibit issuers—including officers, directors, and 20 percent shareholders—from promoting or paying promoters to express opinions outside the platform that would go beyond pointing the public to the funding portal.").

914 A flat fixed fee is one that is not based on the success of the offering, and so would not be transaction-based compensation. We note that the receipt of direct or indirect transaction-based compensation would strongly indicate that the recipient is acting as a broker. As such, the party receiving this kind of compensation needs to consider whether it would be required to register as a broker.

915 *See also* Rule 402 of Regulation Crowdfunding and discussion in Section II.D.3 (discussing advertising and marketing activities in which a funding portal may engage under the Regulation's safe harbor).

would register with the Commission.[916] Securities Act Section 4A(a)(12) requires intermediaries to comply with requirements as the Commission may, by rule, prescribe for the protection of investors and in the public interest. Exchange Act Section 3(h)(1)(C) also permits the Commission to impose, as part of its authority to exempt funding portals from broker registration, "such other requirements under [the Exchange Act] as the Commission determines appropriate."

We proposed to establish a streamlined registration process under which a funding portal would register with the Commission by filing a form with information consistent with, but less extensive than, the information required for broker-dealers on the Uniform Application for Broker-Dealer Registration ("Form BD").[917] Under proposed Rule 400(a), a funding portal would register by completing a Form Funding Portal, which would include information concerning the funding portal's principal place of business, its legal status and its disciplinary history, if any; business activities, including the types of compensation the funding portal would receive; control affiliates of the funding portal and disclosure of their disciplinary history, if any; FINRA membership or membership with any other registered national securities association; and the funding portal's website address(es) or other means of access.[918] Proposed Rule 400(a) also would require a funding portal to become a member of FINRA or another applicable national securities association registered under Exchange Act Section 15A. As proposed in Rule 400(a), the funding portal's registration would become effective the later of: (1) 30 calendar days after the

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916 *Compare* Exchange Act Section 15(b) [15 U.S.C. 78*o*(b)] (prescribing the manner of registration of broker-dealers).

917 Brokers currently register with the Commission using Form BD. Information on that form regarding the broker's credentials, including current registrations or licenses and employment and disciplinary history, is publicly available on FINRA's BrokerCheck.

918 We discuss in Section II.D.1.b the information required to be included in Form Funding Portal.

date that the registration is received by the Commission; or (2) the date the funding portal is approved for membership in FINRA or any other registered national securities association.

Proposed Rule 400(b) would require a funding portal to file an amendment to Form Funding Portal within 30 days of any of the information previously submitted on the form becoming inaccurate for any reason.

In addition, proposed Rule 400(c)(1) would permit a funding portal that succeeds to and continues the business of a registered funding portal to also succeed to the registration of the predecessor on Form Funding Portal. As proposed in Rule 400(c)(1), the registration would remain effective as the registration of the successor if the successor, within 30 days after such succession, files a registration on Form Funding Portal and the predecessor files a withdrawal on Form Funding Portal.[919] Proposed Rule 400(c)(1), therefore, would not apply where the predecessor funding portal intends to continue to engage in funding portal activities.

In certain circumstances, proposed Rule 400(c)(2) would allow the successor to file an amendment to the predecessor's Form Funding Portal rather than requiring the successor and predecessor, respectively, to follow the registration filing and withdrawal process under Rule 400(c)(1) described above. Specifically, proposed Rule 400(c)(2) provides that, if the succession is based solely on a change of the predecessor's date or state of incorporation, form of organization or composition of a partnership, the successor may, within 30 days after the succession, amend the notice registration of the predecessor on Form Funding Portal to reflect these changes. Successions by amendment would be limited to those successions that resulted

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[919] Under the proposed rules, the registration of the predecessor funding portal would be deemed withdrawn 45 days after the notice registration on Form Funding Portal was filed by the successor. *See* proposed Rule 400(c)(1). A similar process exists for registered broker-dealers under Exchange Act Rule 15b1-3 (17 CFR 240.15b1-3).

from a formal change in the structure or legal status of the funding portal but did not result in a change in control.

The instructions to the proposed Form Funding Portal would limit the term "successor" to an entity that assumed or acquired substantially all of the assets and liabilities of the predecessor funding portal's business.

We also proposed in Rule 400(d) to require a funding portal to promptly file a withdrawal of registration on Form Funding Portal upon ceasing to operate as a funding portal. The withdrawal would be effective on the later of 30 days after receipt by the Commission, after the funding portal was no longer operational, or within a longer period of time consented to by the funding portal or that the Commission, by order, determined as necessary or appropriate in the public interest or for the protection of investors.[920]

Proposed Rule 400(e) would provide that each application for registration, amendment thereto, successor registration or withdrawal would be considered filed when a complete Form Funding Portal was submitted with the Commission or its designee. Proposed Rule 400(e) also would require duplicate originals of the application to be filed with surveillance personnel designated by the registered national securities association of which the funding portal is a member.

[920] A similar process exists for registered broker-dealers under Exchange Act Section 15(b)(5) (15 U.S.C. 78*o*(b)(5)) and Rule 15b6-1 (17 CFR 240.15b6-1) thereunder.

(2) Comments on the Proposed Rule

We received some comments generally supporting the proposed registration method,[921] while one commenter generally opposed the proposed registration method, stating the Commission is requiring too stringent a registration process and financial overhead for funding portals.[922] One commenter encouraged the Commission to require broker-dealers to register on the same form as funding portals.[923]

In the Proposing Release, we requested comments on whether we should impose other restrictions or prohibitions on affiliations of the funding portal, such as affiliation with a registered broker-dealer or registered transfer agent. Some commenters opposed the imposition of other restrictions or prohibitions on affiliations of the funding portal.[924] One of these commenters stated that affiliations and partnerships with brokers or transfer agents should be optional.[925]

(3) Final Rules

We are adopting Rule 400(a) – (e) generally as proposed with one change. We are deleting from Rule 400(e) as proposed the language stating that Form Funding Portal may be filed with a Commission designee, as we have determined not to designate this function. Rather, these filings will be made through the EDGAR system as explained in more detail below.

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921 *See, e.g.*, Joinvestor Letter; DreamFunded Letter (favoring the proposed rules which provide a "high barrier to entry" to funding portals, as it will "stop anyone from potentially creating a funding portal over a weekend").

922 *See* PeoplePowerFund Letter (suggesting that the Commission should consider, "a simple registration detailing the owners and operators of a web portal, the legal domicile and registration contact information etc. and the portals [sic] commitment to adherence of the rules of the [C]ommission").

923 *See* RocketHub Letter. The commenter also stated that it has "a serious concern with [broker-dealers] having an unfair advantage in the market, by already being regulated and registered with the Commission as well as FINRA. Therefore, they may be able to service the market well ahead of [funding] [p]ortals."

924 *See, e.g.*, Joinvestor Letter; Tiny Cat Letter.

925 *See* Tiny Cat Letter.

Rule 400 establishes a streamlined registration process for a funding portal to register with the Commission. We have considered the general comment suggesting that the registration requirement for funding portals is too stringent and creates financial overhead. We believe, however, that the rules as adopted provide a reasonable approach to funding portal registration – they are based on broker-dealer registration requirements, which we believe have been effective in providing investor protection and allowing the Commission to perform its oversight function. At the same time, the registration requirement takes into account the more limited activities of funding portals as compared to broker-dealers. As such, the registration requirements we are imposing on funding portals are generally consistent with those imposed on broker-dealers, while not as extensive in every aspect. As we note in Section III.B.5, we have considered the costs of funding portal registration and believe that the anticipated costs to funding portals are justified in light of the expected benefits investors will receive from utilizing funding portals that are subject to registration requirements, which include public disclosure of registration information on Form Funding Portal in EDGAR, as described in more detail in Section II.D.1.b below. We believe that having such a registration system will promote investor confidence in this new and emerging market, while providing us and FINRA (and any other applicable national securities association registered pursuant to Exchange Act Section 15A) with information integral to effective oversight.

Finally, consistent with the proposal, we are not imposing additional restrictions or prohibitions on affiliations of the funding portal in the final rules. We note, however, that Form Funding Portal, which will be publicly available, requires a funding portal to disclose information about its control relationships and the disciplinary history of associated persons.[926]

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[926] *See* Item 4 - Control Relationship of Form Funding Portal and Item 5 – Disclosure Information of Form Funding Portal. "Control" is defined for the purposes of Form Funding Portal as "[t]he power, directly or

b. Form Funding Portal

(1) Proposed Rules

As noted above, proposed Rule 400(a) requires a funding portal seeking to register with the Commission, through an initial application, to file a completed Form Funding Portal with the Commission. As proposed, Rule 400(b) – (d) would have also required funding portals to use proposed Form Funding Portal to amend any part of the funding portal's most recent Form Funding Portal, including certain successor registrations, or to withdraw from registration as a funding portal with the Commission.[927] We proposed to make a blank Form Funding Portal available through the Commission's website or such other electronic database, as determined by the Commission in the future.

As proposed, Form Funding Portal appropriately considered the need to provide efficiency in completing the form while requesting sufficient information from funding portals to allow for effective regulatory oversight. The proposed form would have consisted of eight sections, including items related to: identifying information, form of organization, successions, control persons, disclosure information, non-securities related business, escrow, compensation arrangements, and withdrawal. These items would require an applicant to provide certain basic identifying and contact information concerning its business; list its direct owners and executives;

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indirectly, to direct the management or policies of the *funding portal*, whether through contract, or otherwise. A *person* is presumed to *control* a *funding portal* if that *person*: (1) is a director, general partner or officer exercising executive responsibility (or has a similar status or functions); (2) directly or indirectly has the right to vote 25 percent or more of a class of a voting security or has the power to sell or direct the sale of 25 percent or more of a class of voting securities of the *funding portal*; or (3) in the case of a partnership, has contributed, or has a right to receive, 25 percent or more of the capital of the *funding portal*." *See* Instructions to Form Funding Portal.

927 As noted in Section II.D.1.a., a successor funding portal may amend the registration of its predecessor on Form Funding Portal, within 30 days after succession, if the succession is based solely on a change of the predecessor's date of incorporation, state of incorporation, form of organization, or composition of a partnership. Otherwise, a successor must file a registration statement on Form Funding portal within 30 days after succession and a predecessor must file a withdrawal on Form Funding Portal. *See* Rule 400(c).

identify persons that directly or indirectly control the funding portal, control the management or policies of the funding portal and persons the funding portal controls; and supply information about its litigation and disciplinary history and the litigation and disciplinary history of its associated persons.[928] Under proposed Form Funding Portal, a funding portal would be able to operate multiple website addresses under a single funding portal registration, provided the funding portal disclosed on Form Funding Portal all the websites and names under which it did business.[929] In addition, the proposed form would have required an applicant to describe any non-securities related business activities and supply information about its escrow arrangements, compensation arrangements with issuers and fidelity bond.

Upon a filing to withdraw from registration, a funding portal would be required to provide certain books and records information. In addition, as discussed in detail in Section II.D.1.d. below, applicants that are incorporated in or organized under the laws of a jurisdiction outside of the United States or its territories, or whose principal place of business is not in the United States or its territories, would have been required to complete Schedule C to Form Funding Portal, which would require information about the applicant's arrangements to have an agent for service of process in the United States, as well as a certification and an opinion of counsel addressing the ability of the applicant to provide the Commission and the national securities association of which it is a member with prompt access to its books and records and to submit to onsite inspection and examination by the Commission and the national securities association.

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928 This information would be used to determine whether to approve an application for registration, to decide whether to revoke registration, to place limitations on the applicant's activities as a funding portal and to identify potential problem areas on which to focus during examinations. If an applicant or its associated person has a disciplinary history, then the applicant could be required to complete the appropriate Disclosure Reporting Page ("DRP"), either Criminal, Regulatory, Civil Judicial, Bankruptcy, Bond or Judgment on proposed Form Funding Portal.

929 *See* proposed Form Funding Portal, Item 1; 17 CFR 249.2000.

We also proposed that a person duly authorized to bind the funding portal be required to sign Form Funding Portal in order to execute the documents.[930] As proposed, the funding portal also would have been required to consent to service of process to its contact person on the form.[931]

Finally, we proposed to make all current Forms Funding Portal, including amendments and registration withdrawal requests, immediately accessible and searchable by the public, with the exception of certain personally identifiable information or other information with significant potential for misuse (including the contact employee's direct phone number and e-mail address and any IRS Employer Identification Number, social security number, date of birth, or any other similar information).[932]

(2) Comments on Proposed Rules

We received one comment in support of using EDGAR for all funding portal filing and registration requirements.[933] Some commenters also generally supported allowing a funding portal to file one registration application to operate multiple websites.[934] One commenter, however, expressed concern about allowing funding portals to file one registration form for

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930 *See* execution statement of proposed Form Funding Portal. We proposed requiring a person executing Form Funding Portal and Schedule C (if applicable) to represent that the person has executed the form on behalf of, and is duly authorized to bind, the funding portal; the information and statements contained in the form and other information filed are current, true and complete; and if the person is filing an amendment, to the extent that any information previously submitted is not amended, such information is currently accurate and complete.

931 *See* execution statement of proposed Form Funding Portal. Specifically, we proposed requiring the funding portal to consent that service of any civil action brought by, or notice of any proceeding before, the Commission or any national securities association of which it is a member, in connection with the funding portal's investment-related business, may be given by registered or certified mail to the funding portal's contact person at the main address, or mailing address, on the form.

932 *See* proposed Instructions to Form Funding Portal.

933 *See* Public Startup Letter 3.

934 *See, e.g.*, Joinvestor Letter; Tiny Cat Letter (stating that requiring new applications for each website would be unnecessary as it "would not provide any new information for either the commission or the public" so long as the expansion involves no material changes to information in the initial application).

multiple websites. This commenter suggested the Commission "clearly address Portals that register with the Commission, and then subsequently license out or sell their registration."[935] The same commenter stated that "[s]ome entrepreneurs have indicated that they intend to operate a 'parent' funding [p]ortal, which allows other sites to operate under its umbrella, (leveraging the parent's systems, architecture, design, infrastructure, etc.)."[936]

(3) Final Rules

We are adopting Form Funding Portal generally as proposed,[937] with the following changes:

- The final rules amend Regulation S-T to permit a funding portal to file PDF exhibits and attachments to Form Funding Portal on EDGAR as "official filings."[938]
- The following has been added to the title of the form: "Application or Amendment to Application for Registration or Withdrawal from Registration as Funding Portal" to clarify that the form will be used for all funding portal registration applications, amendments and withdrawals;
- Amendments to Form Funding Portal will require a narrative explaining the amendment, which we believe will clarify to investors and potential investors the particular information being amended by the funding portal in its filing;

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935 RocketHub Letter.

936 *Id*.

937 We also made minor non-substantive technical changes and changes to increase the clarity of the information being requested in the form.

938 *See* Rule 101(a)(1)(xviii) of Regulation S-T. As we noted in Section II.B.3, Regulation S-T generally allows PDF documents to be filed only as unofficial copies. *See* Rule 104 of Regulation S-T. However, Rule 101 provides for certain exceptions to this restriction. The PDF documents must be in the format required by the EDGAR Filer Manual, as defined in Rule 11 of Regulation S-T.

- Form Funding Portal will not require information about fidelity bonds since we are not adopting the fidelity bond requirement in the proposed rules;[939]
- Item 1 also will require information about website URL changes on the most recent Form Funding Portal, title of the contact employee and the month the applicant funding portal's fiscal year ends;
- The title of Item 4 is changed from "Control Persons," as proposed, to "Control Relationships," as adopted, to clarify that Item 4 may capture information not being captured in Schedules A and B;
- The language in Item 5 "to determine whether to approve an application for registration" has been deleted;[940]
- Item 7, as adopted, references "qualified third party arrangements" rather than "escrow arrangements," as proposed, to indicate that, in addition to holding the funds in escrow, a qualified third party may also hold investor funds in an account for the benefit of investors and the issuer;[941]
- "G – Other (general partner, trustee, or elected member)" has been added as an ownership code in Schedule A;
- Schedules A and B have been changed from the proposal to clarify that the Schedules are collecting information about whether direct owners and executive officers are "control" persons;

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939 *See* Section II.D.1.c.

940 We note, however, that failure to answer a question in Item 5 will result in an incomplete application for registration.

941 *See* Section II.C.5.e.

- The language to Schedule C of Form Funding Portal has been changed to track more closely the requirements of Rule 400(f) for nonresident funding portals and to add an execution section for these entities; and
- Withdrawal information for funding portals proposed to be collected under Item 8 will instead be collected in a new "Schedule D".[942]

We continue to believe that the information required by Form Funding Portal is important for our oversight of funding portals and to allow us to assess a funding portal's application for registration and perform examinations of funding portals. We also note that the information required by the Form will be available to investors and potential investors and will provide transparency regarding intermediaries. Although we generally modeled Form Funding Portal on Form BD, we have tailored the questions to the activities of funding portals. For example, Form Funding Portal, in contrast to Form BD, does not include any questions about holding customer funds and securities because funding portals are statutorily prohibited from holding or maintaining customer funds or securities. We also included questions in Form Funding Portal to address specific restrictions that are imposed upon funding portals but not upon broker-dealers. For example, Form Funding Portal requires specific information about a funding portal's qualified

[942] There have been no substantive changes to the withdrawal information to be collected on Schedule D. The instructions to Form Funding Portal have been modified from the proposal to (1) include IRS Tax Identification Number and the contact employee's fax number as information that will be redacted on Form Funding Portal by the Commission and, therefore, not disseminated to the public by the form; and (2) inform funding portals that they should manually redact certain personally identifiable information or other information with significant potential for misuse (including the contact employee's direct phone number, fax number and e-mail address and any IRS Employer Identification Number, IRS Tax Identification Number, social security number, or any other similar information) from any PDF attachments they file as part of their Form Funding Portal submission due to privacy concerns. The instructions have also been modified to amend the definition of SRO to delete the reference to Section 3 of the Exchange Act and clarify that the phrase "any national securities association registered with the Commission" in the definition encompasses any national securities association registered under Section 15A of the Exchange Act, in order to alleviate any confusion by funding portals when completing the form.

third party arrangements because a funding portal is prohibited from holding and maintaining customer funds.

In developing these requirements, we have taken into account that funding portals are limited purpose brokers that are conditionally exempt from registration as broker-dealers, and accordingly have sought to require appropriate information from these entities, while, at the same time, not making the process of completing and filing the required form inappropriately burdensome for funding portals.

As noted above, we proposed to make a blank Form Funding Portal available through our website or another electronic database. At the time of the Proposing Release, we had not yet determined the appropriate database through which to access and electronically file Form Funding Portal. We requested comments in the Proposing Release on the type of web-based registration that funding portals should use for accessing and filing Form Funding Portal, and as noted above, received one comment in support of using EDGAR for funding portal filing and registration requirements.[943] We have determined to require funding portals to access and file Form Funding Portal through the Commission's EDGAR system. Before a funding portal will be able to access EDGAR and electronically file Form Funding Portal, it will have to obtain EDGAR access codes and a central index key ("CIK") by creating and submitting a Form ID with the Commission for authorization to access EDGAR. The applicant will be required to fill out general user information fields on Form ID, including filer type name, address, phone number, e-mail address, organization name and employer identification number and file a signed, notarized version of the document. To facilitate this process, we are amending Form ID to add "Funding Portal" as a filer type and are also revising the instructions to the form to include the definition of "funding portal"

[943] *See* Public Startup Letter 3.

(as defined by Rule 300(c)(2)). Once the application has been accepted by the Commission, the funding portal will receive an e-mail with a CIK, which it can use (along with a passphrase that it has previously created) to generate EDGAR access codes, and access the system and Form Funding Portal.

As proposed, a funding portal will be required to check a box indicating the purpose for which the funding portal was filing the form:

- to register as a funding portal with the Commission, through an initial application;
- to amend any part of the funding portal's most recent Form Funding Portal, including a successor registration; or
- to withdraw from registration as a funding portal with the Commission.

The funding portal will receive an SEC file number after it files its Form Funding Portal initial application, and thereafter must provide us that file number when submitting an amendment or withdrawal from registration on Form Funding Portal. We will use this number to cross-reference amendments and withdrawals to the original registration.

When a funding portal's registration becomes effective, the information on Form Funding Portal will be made available to the public through EDGAR, with the exception of certain personally identifiable information or other information with significant potential for misuse (including the contact employee's direct phone number, fax number and e-mail address and any IRS Employer Identification Number, IRS Tax Identification Number, social security number, date of birth or any other similar information). In addition to current versions of Form Funding Portal, investors and potential investors also will be able to access historical versions of a funding portal's filings on EDGAR. We believe that making these documents publicly available and

searchable will provide the public with information about the registration process and the funding portal industry, thereby increasing transparency into this developing market.

The final rule permits a funding portal to operate multiple website addresses under a single funding portal registration. As we noted in the Proposing Release, we believe that allowing a funding portal to utilize more than one website address, if it chooses to do so, may allow the portal to minimize its regulatory costs while having the flexibility to customize each website to fit its specific needs, such as appealing to certain industries or investors. We have considered one commenter's concern about funding portals licensing or selling their registrations, and note that registrations are not transferrable among entities; rather, each funding portal is required to register with the Commission, pursuant to Rule 400(a). As explained above, an entity may succeed to and continue the business of a registered funding portal, but the successor must file a registration on Form Funding Portal within 30 days after any succession resulting in a change of control.[944]

c. Fidelity Bond

(1) Proposed Rule

Proposed Rule 400(f) would have required that funding portals, as a condition of registration, have in place, and thereafter maintain for the duration of such registration, a fidelity bond that: (1) has a minimum coverage of $100,000; (2) covers any associated person of the funding portal unless otherwise excepted in the rules set forth by FINRA or any other registered national securities association of which it is a member; and (3) meets any other applicable requirements set forth by FINRA or any other registered national securities association of which it is a member. While fidelity bond coverage was not mandated by statute, the proposed requirement was intended to help insure against the loss of investor funds that might occur if a

[944] *See* Section II.D.1.a.

funding portal were to violate the express prohibition set forth in Exchange Act Section 3(a)(80) on holding, managing, possessing or otherwise handling investor funds or securities.

(2) Comments on Proposed Rule

We received comments both in support of,[945] and opposition to,[946] the proposed requirement for funding portals to maintain fidelity bonds. One commenter stated its view that a fidelity bond may be necessary as a preventative measure to protect the interests of investors and issuers.[947] Another commenter noted that although fidelity bond coverage may be "indirect" to customers, they are protected under such coverage because the insured entity may recover its losses due to theft or embezzlement by its employees and meet the obligations of its customers.[948] The same commenter, however, suggested that the Commission may find a surety bond more appropriate in the crowdfunding context than a fidelity bond because investors would be able to make a direct claim under it for losses due to a funding portal's violation of the rules, and the insurer would be able to seek indemnity for that amount from the funding portal.[949] One commenter stated that it is not appropriate to require that the fidelity bond cover associated persons, and that the requirement is a "hangover from a non-transparent financial services sector," unlike the transparent crowdfunding model.[950] Another commenter noted that a fidelity bond would protect a funding portal from employee theft or embezzlement, and suggested that there is a low risk of this occurring since a funding portal not does hold cash or customer funds.[951] The

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945 *See, e.g.*, Joinvestor Letter; Public Startup 3 Letter; RocketHub Letter; SFAA Letter.

946 *See, e.g.*, ASSOB Letter; Heritage Letter; PeoplePowerFund Letter; RoC Letter.

947 *See* Joinvestor Letter.

948 *See* SFAA Letter.

949 *See id*.

950 *See* ASSOB Letter.

951 *See* Heritage Letter

commenter further stated that "[o]btaining a bond is simply one more expense that the portal must incur and it is necessary to control compliance costs if crowdfunding is to be a success."[952]

(3) Final Rules

After taking into account the comments and upon further consideration, we have determined not to adopt a fidelity bond requirement for funding portals. We have been persuaded by the comments that such a requirement may not be appropriate. We believe that the statutory protections and prohibitions set forth in Exchange Act Section 3(a)(80) on holding, managing, possessing or otherwise handling investor funds or securities provide substantial protections to investors. We recognize, as some commenters observed, that there may be potential risks to investors if a funding portal were to violate the prohibitions in Regulation Crowdfunding, including the potential loss of investor funds. As we discussed in the Proposing Release, funding portals will not be members of the Securities Investor Protection Corporation ("SIPC") and their customers, therefore, will not receive SIPC protection.[953] Furthermore, consistent with the proposed rules, the final rules also do not subject funding portals to minimum net capital requirements. Despite these vulnerabilities, we note that the potential burden associated with the requirement of a fidelity bond (or any bond) may not be justified by the benefits that could be derived from requiring that a funding portal obtain such a bond. In particular, we are concerned that a fidelity bond requirement could create a potential barrier to entry for some funding portals that could be detrimental to our mission of capital formation, as well as the feasibility of crowdfunding. At the same time, we are mindful of the potentially limited benefits of requiring such bonds to be obtained by funding portals, when taking into account the statutory restrictions

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952 *Id.*

953 *See* Proposing Release at 78 FR at 66482. Membership in SIPC applies only to persons registered as brokers or dealers under Section 15(b) of the Exchange Act. *See* 15 U.S.C. 78ccc(a)(2).

on funding portals' permissible activities. Instead, we believe at this time that the prohibition on a funding portal from handling customer funds and securities as well as the general anti-fraud provisions of our statutes and rules provide significant investor protections that do not need to be supplemented by a fidelity bond requirement. This decision is consistent with our approach generally to the regulation of funding portals in which we have sought to structure rules tailored to the business of funding portals that address the risks posed by such activities while considering the impact that our rules may have on this emerging market.

d. Requirements for Nonresident Funding Portals

(1) Proposed Rules

Under proposed Rule 400(g), registration pursuant to Rule 400 of Regulation Crowdfunding by a "nonresident funding portal"[954] would be first conditioned upon there being an information sharing arrangement in place between the Commission and the competent regulator in the jurisdiction under the laws of which the nonresident funding portal is organized or where it has its principal place of business that is applicable to the nonresident funding portal. The proposed rule would further require a nonresident funding portal registered or applying for registration to: (1) obtain a written consent and power of attorney appointing an agent for service of process in the United States (other than the Commission or a Commission member, official or employee), upon whom may be served any process, pleadings, or other papers in any action;[955] (2) furnish the Commission with the name and address of its agent for services of process on

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954 *See* proposed Rule 400(g)(1) of Regulation Crowdfunding (defining "nonresident funding portal" as "a funding portal incorporated in or organized under the laws of any jurisdiction outside of the United States or its territories, or having its principal place of business in any place not in the United States or its territories").

955 *See* proposed Rule 400(g)(2)(i) of Regulation Crowdfunding.

Schedule C of Form Funding Portal;[956] and (3) certify on Schedule C of Form Funding Portal and provide an opinion of counsel that it can, as a matter of law, provide the Commission and any national securities association of which it is a member with prompt access to its books and records and can, as a matter of law, submit to onsite inspection and examination by the Commission and such national securities association.[957]

Proposed Rule 400(g)(2)(iv) would require a registered nonresident funding portal to promptly appoint a successor agent if it discharges its identified agent for service of process or if its agent for service of process is unwilling or unable to accept service on its behalf. In addition, proposed Rule 400(g)(2)(iii) would require a registered funding portal to promptly amend Schedule C to its Form Funding Portal if its agent, or the agent's name or address, changes. Finally, proposed Rule 400(g)(2)(v) would require the registered nonresident funding portal to maintain, as part of its books and records, the agreement with the agent for service of process for at least three years after termination of the agreement.

In addition, we proposed in Rule 400(g)(3)(ii) to require a registered nonresident funding portal to re-certify, on Schedule C to Form Funding Portal, within 90 days after any changes in the legal or regulatory framework that would affect: (1) its ability to provide (or the manner in which it provides) the Commission, or the national securities association of which it is a member, with prompt access to its books and records; or (2) the ability of the Commission or the national securities association to inspect and examine the nonresident funding portal. The re-certification would be accompanied by a revised opinion of counsel describing how, as a matter of law, the

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956 *See* proposed Rule 400(g)(2)(ii) of Regulation Crowdfunding.

957 *See* proposed Rule 400(g)(3)(i) of Regulation Crowdfunding. Exchange Act Section 3(h)(1)(C) permits us to impose, as part of our authority to exempt funding portals from broker registration, "such other requirements under [the Exchange Act] as the Commission determines appropriate."

entity can continue to meet its obligations to provide the Commission and the national securities association with prompt access to its books and records and to be subject to inspection and examination.[958]

(2) Comments on the Proposed Rule

One commenter stated its view that the definition of a nonresident funding portal will create a competitive advantage for foreign intermediary platforms.[959] Another commenter stated its view that nonresident funding portals should be subject to the same rules as domestic funding portals.[960]

In the Proposing Release, we requested comments about other actions or requirements that could address our concern that the Commission and the applicable national securities association be able to have direct access to books and records and be able to adequately examine and inspect a nonresident funding portal, if it would be impossible or impractical for such funding portal to obtain the required opinion of counsel. In response, a commenter suggested an arrangement between a nonresident funding portal and a domestic funding portal in which the nonresident funding portal would be required to make and keep current books and records, but the domestic

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958 *See* proposed Rule 400(g)(3)(ii) of Regulation Crowdfunding.

959 *See* Public Startup Letter 3 (stating its view that the definition of nonresident funding portal is "flawed" because it believes these foreign entities could choose to act as intermediaries for U.S. issuers and U.S. investors in crowdfunding transactions without relying on Section 4(a)(6) and, therefore, gain a competitive advantage by not having to comply with the requirements of the rules under Regulation Crowdfunding in the same manner as domestic funding portals). *But see* Joinvestor Letter (stating its belief that "nonresident funding portal is properly defined").

960 *See* Wales Capital Letter 3. The commenter also recommended using the term "'foreign' funding portal" to be consistent with the treatment of corporations incorporated in another jurisdiction under various state laws. According to the commenter, a foreign corporation must file a notice of doing business in any state or nation in which it does substantial regular business, and must name an "'agent for acceptance of service'" in that nation (or the Secretary of State as agent) to allow people doing business with a foreign corporation to be able bring legal actions locally.

funding portal would have the ability to obtain and be responsible for the accuracy of such books and records.[961]

One commenter suggested that nonresident funding portals be required to clearly indicate on their websites that they are organized and operating outside of the U.S. and indicate whether a U.S. or non-U.S. bank will be used to process investors' funds.[962] One commenter suggested that a nonresident funding portal should be required to appoint a U.S. agent for all potential proceedings,[963] while another commenter suggested that a nonresident funding portal should be required to have a resident legal representative to handle any matters between issuers or investors and the portal.[964]

(3) Final Rules

We are adopting Rule 400(g) as proposed with certain minor changes, and renumbering it as Rule 400(f) due to the elimination of the fidelity bond requirement proposed as subparagraph (f).[965] We are changing the language of the rule as adopted applicable to a nonresident funding portal to:

- Add the term "registered" to any references to national securities association in the Rule to be more consistent with the terminology in the Exchange Act; and
- Require the nonresident funding portal also to certify that it "will" provide the Commission and any national securities association of which it "becomes" (rather

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961 *Id.*

962 *See* Zhang Letter.

963 Wales Capital Letter 3.

964 *See* Joinvestor Letter.

965 We also added "*Inspections and Examinations*" to the heading of Rule 400(f)(3); this modification does not change the requirements from those proposed. In addition, we changed a cross-cite in the rule text to reflect the renumbering.

than "is") a member with prompt access to the books and records and "will" submit to onsite inspection and examination by the Commission and such national securities association.[966]

As we noted in the Proposing Release, the rule aims to help ensure that we and any applicable registered national securities association can access the books and records of, conduct examinations and inspections of, and enforce U.S. laws and regulations with respect to, funding portals that are not based in the United States, or that are subject to laws other than those of the United States. We believe that these rules will further our goal of promoting the ability of the Commission and any applicable national securities association to conduct effective regulatory oversight of funding portals.

We have considered the comments and believe that the final rule appropriately takes into consideration the need to provide more choices for U.S. issuers seeking to use intermediaries or access investors outside of the United States, while meeting the challenges associated with supervising, examining, and enforcing rules regarding activities of intermediaries based outside the United States. For example, as we noted in the Proposing Release, the requirement for an information sharing arrangement is designed to provide us with greater assurance that we will be able to obtain information about a nonresident funding portal necessary for our oversight of the funding portal. The ability to obtain information and secure the cooperation of the home country regulator according to established practices and protocols is expected to help to address the increased challenges that may arise from oversight of entities located outside of the United States.

[966] The language in the proposed rule required a certification that the funding portal "can" meet such obligations but did not require a certification that it "will" meet them.

We note that nonresident funding portals are subject to the same registration requirements as other funding portals under Rule 400.[967]

We have also considered the comment submitted in response to our question about the use of books and records arrangements in situations where it would be impossible or impractical for a nonresident funding portal to obtain the required opinion of counsel.[968] We have determined not to adopt an alternative to the opinion of counsel requirement for nonresident funding portals in Regulation Crowdfunding. The opinion of counsel requirement is consistent with our approach to other nonresident registered entities and we believe it is an appropriate mechanism to use here, as well.[969] As we stated in the Proposing Release, we believe that the certification and supporting opinion of counsel requirements are important to confirm that each nonresident funding portal is in a position to provide the Commission and FINRA (or the applicable national securities association registered under Exchange Act Section 15A) with information that is necessary for us and the national securities association to effectively fulfill regulatory oversight responsibilities.[970] We do not believe that the books and records arrangement suggested by the commenter would provide assurance that we or FINRA would be able to consistently obtain such information, which could hinder our ability to fulfill our regulatory oversight responsibilities.

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967 We have considered the commenter's view that there would be a potential competitive advantage for foreign intermediaries choosing to operate outside of the Section 4(a)(6) exemption. *See* Public Startup Letter 3. However, we note that any entities (foreign or domestic) intermediating offerings of securities between U.S. issuers and investors generally will be broker-dealers, either required to register under the Exchange Act or to be exempt from registration. *See* 15 U.S.C. 78o(a). We also note that the offer and sale of securities in the United States or to U.S. persons must be registered unless an exemption is available.

968 *See* Wales Capital Letter 3.

969 We note that the opinion of counsel requirement is generally consistent with the requirement for nonresident security-based swap dealers and major security-based swap participants, as well as those for nonresident municipal advisors. *See* Exchange Act Rule 15Fb2-4 and Rule 15Ba1-6.

970 *See* Exchange Act Section 3(h)(1)(A). Failure to make this certification or re-certification or to provide an opinion of counsel or revised opinion of counsel will result in an incomplete application for registration.

We have also considered the comment suggesting that a nonresident funding portal be required to clearly indicate on its website that it is organized and operating outside of the United States and whether it will use a U.S. or non-U.S. bank to process investors' funds.[971] However, in light of the other disclosure requirements we are adopting, we are not persuaded that such a requirement is necessary. We note that the information required to be filed on Form Funding Portal (and that will be publicly disclosed) will include information about the qualified third party for the maintenance and transmission of investors' funds under Rule 303(e), including the name and address of the qualified third party.[972] In addition, a nonresident funding portal will be required to publicly disclose information on Schedule C to Form Funding Portal. Since Schedule C is required to be completed by nonresident funding portals only, investors will be able to discern easily whether or not the entity is a nonresident funding portal and, among other things, has certified (and provided an attached opinion of counsel indicating) that it is able to provide the Commission and any national securities association prompt access to its books and records and will submit to onsite inspection and examination by the same.

Finally, we have considered the comments suggesting that a nonresident funding portal should be required to have a U.S. agent for potential proceedings,[973] or a resident legal representative to handle any matters between issuers or investors, and the portal.[974] We note that, as discussed above, we are requiring funding portals to execute a written consent and power of attorney appointing an agent in the United States. The agent will be the representative of the funding portal for service of any process, pleadings or other papers in any action to enforce the

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971 *See* Zhang Letter.

972 *See* Form Funding Portal, Item 7 - Qualified Third Party Arrangements; Compensation Arrangements.

973 *See* Wales Capital Letter 3.

974 *See* Joinvestor Letter.

Exchange Act, Securities Act or any rule or regulation promulgated thereunder. As we noted above, we have limited the types of actions for which a nonresident funding portal will be required to have an agent for service of process, pleadings, or other papers in order to remain generally consistent with recent requirements that we have imposed on other types of nonresident entities. The funding portal will be required to disclose the name and address of its U.S. agent in Schedule C to its Form Funding Portal, and amend the Schedule promptly upon any change to the agent, agent's name or agent's address. We are not, however, requiring that nonresident funding portals have a resident legal representative to handle any matters between the portal and issuers or investors, which is consistent with our approach to other nonresident registered entities.[975]

2. Exemption from Broker-Dealer Registration

a. Proposed Rule

Exchange Act Section 3(h)(1), which was added by Section 304(a) of the JOBS Act, directs the Commission by rule to exempt, conditionally or unconditionally, a registered funding portal from the requirement to register as a broker or dealer under Exchange Act Section 15(a), provided that the funding portal: (1) remains subject to the examination, enforcement and other rulemaking authority of the Commission; (2) is a member of a registered national securities association; and (3) is subject to other requirements that the Commission determines appropriate.

As explained earlier, the role contemplated by Title III of the JOBS Act for an entity acting as an intermediary in a crowdfunding transaction would bring that entity within the

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975 For example, we note that requiring a U.S. agent for service of process but not requiring a U.S. legal representative to handle any matters between a funding portal and issuers or investors is generally consistent with the requirements for nonresident security-based swap dealers and major security-based swap participants, as well as those for nonresident municipal advisors. *See* Exchange Act Rule 15Fb2-4 and Rule 15Ba1-6.

definition of "broker" under Exchange Act Section 3(a)(4).[976] A funding portal would be "effecting transactions in securities for the account of others" by, among other things, ensuring that investors comply with the conditions of Securities Act Section 4A(a)(4) and (8), making the securities available for purchase through the funding portal, and ensuring the proper transfer of funds and securities as required by Securities Act Section 4A(a)(7).[977] In addition, a funding portal's receipt of compensation linked to the successful completion of the offering also would be indicative of acting as a broker in connection with these transactions. Thus, absent an exemption or exception, a funding portal would be required to register as a broker under the Exchange Act.

We proposed Rule 401(a) to provide an exemption for registered funding portals from the broker registration requirements of Exchange Act Section 15(a)(1) in connection with its activities as a funding portal. Consistent with the JOBS Act, the funding portal would remain subject to the full range of our examination and enforcement authority, even though it is not registered as a broker.[978] In this regard, proposed Rule 403 would require that a funding portal permit the examination and inspection of all of its business and business operations that related to its

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976 *See* Exchange Act Section 3(a)(4)(A) [15 U.S.C. 78c(a)(4)(A)] (defining "broker" as "any person engaged in the business of effecting transactions in securities for the account of others"). An entity acting as an intermediary in the offer and sale of securities pursuant to Section 4(a)(6), as contemplated in Title III of the JOBS Act, would not come within the meaning of "dealer," which is defined in Exchange Act Section 3(a)(5)(A) (15 U.S.C. 78c(a)(4)(A)), because it would not be engaging in the business of buying and selling securities for its own account. *See also* Exchange Act Section 15(a) [15 U.S.C. 15*o*(a)].

977 At the same time, there are statutory restrictions on the scope of services that a funding portal could provide. *See* Section II.C.1 (discussing Exchange Act Section 3(a)(80)).

978 *See* Exchange Act Section 3(h)(1)(C). *See also* Securities Act Section 20 [15 U.S.C. 77t] and Exchange Act Sections 21 and 21C [15 U.S.C. 78u and 78u-3]. In addition, we highlighted in the Proposing Release that Exchange Act Sections 15(b)(4) and 15(b)(6) (15 U.S.C. 78*o*(b)(4) and 78*o*(b)(6)) apply to brokers (including funding portals) regardless of whether or not they are registered with the Commission as brokers. Exchange Act Section 15(b)(4) authorizes the Commission to bring administrative proceedings against a broker when the broker violates the federal securities laws (and for other misconduct) and provides for the imposition of sanctions, up to and including the revocation of a broker's registration. Exchange Act Section 15(b)(6) provides similar enforcement authority against the persons associated with a broker, including barring persons from associating with any Commission registrant.

activities as a funding portal, such as its premises, systems, platforms and records, by representatives of the Commission and of the national securities association of which it is a member.[979] Proposed Rule 404 also would impose certain recordkeeping requirements on funding portals.[980]

We had further proposed in Rule 401(b) that, notwithstanding the exemption from broker registration, for purposes of Chapter X of Title 31 of the Code of Federal Regulations, a funding portal would be a broker or dealer "required to be registered" with the Commission under the Exchange Act, thereby requiring funding portals to comply with Chapter X, including certain anti-money laundering ("AML") provisions thereunder.[981]

b. Comments on the Proposed Rule

Commenters generally agreed with the funding portal exemption from registration as a broker-dealer.[982] One commenter stated that funding portals that provide no advice, make no warranties as to the suitability of an investment and do not handle share transfers or money, should not be required to register as a broker-dealer and requiring them to do so would provide no benefit to the public.[983]

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979 *See* Section II.D.4.

980 *See* Section II.D.5.

981 *See* 31 CFR 1010.100(h) and 1023.100(b) (defining broker or dealer for purposes of the applicability of AML requirements). *See* Currency and Foreign Transactions Reporting Act of 1970 (commonly referred to as the Bank Secrecy Act ("BSA")) [12. U.S.C. 1829b, 12 U.S.C. 1951-1959, 31 U.S.C. 5311-5330].

982 *See, e.g.*, Heritage Letter; Joinvestor Letter; PeoplePowerFund Letter; RocketHub Letter.

983 *See, e.g.*, PeoplePowerFund Letter (stating that requiring funding portals "to register as broker dealers thus crushing the very idea of crowd sourced funding as a people driven force for the good of the 'everyman'").

One commenter stated that the exemption from broker-dealer registration actually precludes funding portals from becoming members of FINRA,[984] and asserted that funding portals should not have to comply with the same requirements as broker-dealers for purposes of Chapter X of Title 31 of the CFR.[985] Another commenter, however, stated that it "supports the Commission's interpretation of the exemption, and believes that AML compliance is necessary."[986]

c. Final Rules

We are adopting, as proposed, paragraph (a) under Rule 401, but renumbering it as Rule 401 as we not adopting proposed Rule 401(b). We note, however, that the exemption from broker registration is applicable only to funding portals that are registered under Rule 400. Therefore, a funding portal that ceases to be registered under Rule 400 will no longer be exempt from broker registration under Rule 401. In response to the comment that this exemption precludes funding portals from becoming members of FINRA, as we noted above, because a funding portal will be engaged in the business of effecting securities transactions for the accounts of others through crowdfunding, it will be a "broker" within the meaning of Section 3(a)(4) of the Exchange Act. We also note that Exchange Act Section 3(h)(2) states that for purposes of sections 15(b)(8) and 15A, the term "broker or dealer" includes a funding portal and the term "registered broker or dealer" includes a registered funding portal. Therefore, funding portals are explicitly permitted by statute to become members of FINRA.

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984 *See* Vann Letter (reasoning that, because a funding portal is "not registered as a 'broker dealer,'" and because "the Securities Exchange Act of 1934 states 'A registered securities association shall deny membership to any person who is not a registered broker or dealer,'" then funding portals cannot become members of FINRA).

985 *Id.* (arguing that such requirements would be "overly burdensome" because funding portals "do not, by law, handle any money").

986 *See* RocketHub Letter.

We are not, however, adopting proposed Rule 401(b). As described in more detail in Section II.D.4.b. below, we have determined that the imposition of AML requirements on funding portals should be addressed outside of the rules that we are adopting in this release.

3. Safe Harbor for Certain Activities

Under Exchange Act Section 3(a)(80), which was added by Section 304(b) of the JOBS Act, a funding portal is defined as an intermediary that does not: (i) offer investment advice or make recommendations; (ii) solicit purchases, sales or offers to buy the securities offered or displayed on its platform or portal; (iii) compensate employees, agents or other persons for such solicitation or based on the sale of securities displayed or referenced on its platform or portal; (iv) hold, manage, possess or otherwise handle investor funds or securities; or (v) engage in such other activities as the Commission, by rule, determines appropriate. As noted in the Proposing Release, commenters have raised questions about the scope of permissible activities for funding portals consistent with these prohibitions.[987] To provide regulatory clarity, we proposed Rule 402, which would provide a non-exclusive conditional safe harbor for funding portals under which certain limited activities would be deemed consistent with the statutory prohibitions on funding portals. The permissible activities in the proposed safe harbor involved: (i) limiting offerings on the platform; (ii) highlighting and displaying offerings on the platform; (iii) providing communication channels; (iv) providing search functions; (v) advising issuers; (vi) compensating others for referring persons to the funding portal; (vii) paying or offering to pay compensation to registered brokers or dealers; (viii) receiving compensation from a registered broker or dealer; (ix) advertising the funding portal and offering; (x) denying access to, or cancelling, offerings due to fraud or investor protection concerns; (xi) accepting investment commitments on behalf of the

[987] *See* Proposing Release 78 FR 66484-66485.

issuer; (xii) directing the transmission of investor funds; and (xiii) directing a qualified third party's transmission of investor funds.

Proposed Rule 402(a) also stated that no presumption shall arise that a funding portal has violated the prohibitions under Section 3(a)(80) of the Exchange Act or Regulation Crowdfunding by reason of the funding portal or its associated persons engaging in activities in connection with the offer or sale of securities in reliance on Section 4(a)(6) of the Securities Act that do not meet the conditions specified in the safe harbor, and that the antifraud provisions and all other applicable provisions of the federal securities laws continue to apply to the activities described in the safe harbor.

Commenters strongly supported the idea of a safe harbor for funding portals,[988] but they also suggested additional examples for the safe harbor. We are adopting the safe harbor in Rule 402 with certain changes as discussed further below. Each activity of the safe harbor is addressed below.

a. Limiting Offerings

(1) Proposed Rule

Proposed Rule 402(b)(1) would permit a funding portal to apply objective criteria to limit the securities offered in reliance on Section 4(a)(6) of the Securities Act through the funding portal's platform where: (i) the criteria are reasonably designed to result in a broad selection of issuers offering securities through the funding portal's platform, are applied consistently to all potential issuers and offerings and are clearly displayed on the funding portal's platform; and (ii) the criteria could include, among other things, the type of securities being offered (for example,

[988] *See, e.g.*, CFIRA Letter 1; Joinvestor Letter; Merkley Letter (stating that the proposed safe harbor "strikes the right balance"). *But see* Public Startup 3 Letter (stating that the safe harbor should cover any activity by a funding portal not directly related to the sale of securities for the account of others).

common stock, preferred stock or debt securities), the geographic location of the issuer and the industry or business segment of the issuer, *provided* that a funding portal may not deny access to an issuer based on the advisability of investing in the issuer or its offering, except to the extent described in proposed Rule 402(b)(10) for fraud and investor protection concerns.

(2) Comments on Proposed Rule

We received a significant number of comments on the ability of a funding portal to limit the offerings on its platform. Many of these comments suggested a broader standard than the standard that we proposed. Several commenters expressed concern that the proposed safe harbor placed funding portals at a competitive disadvantage to registered brokers because it did not provide funding portals with the flexibility to limit the offerings on their platforms,[989] even if they have legitimate concerns about offerings aside from fraud or investor protection.[990] For example, commenters suggested that a funding portal should be permitted to reject offerings based on whatever factors the portal deems appropriate without automatically triggering regulation as a broker-dealer,[991] especially if it deems the offering to have tangible shortcomings that could be detrimental to investors or overly risky.[992]

Commenters asserted that a funding portal's ability to limit the offerings on its platform is important for investor protection. They stated that funding portals should be permitted to screen

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989 *See, e.g.*, EMKF Letter; SBA Office of Advocacy Letter.

990 *See, e.g.*, ABA Letter; CfPA Letter; CrowdCheck 2 Letter; Graves Letter; Seyfarth Letter (stating that "even with a lower liability threshold, curation is an essential tool for investor protection").

991 *See, e.g.*, IAC Recommendation (suggesting that "[o]ne of the most cost-effective ways to reduce the risk of serious compliance violations is to give crowdfunding intermediaries a free hand to reject any offering they believe could pose an undue compliance or fraud risk"); *see also* CFIRA Letter 12 (agreeing with IAC's suggestion "that all intermediaries . . . should have greater latitude in their ability to curate offerings. . . . All intermediaries (including non-BD portals) should be allowed to use their discretion as to whether or not any particular offering is suitable for their service"). *See also* BetterInvesting Letter.

992 *See* Graves Letter.

out clearly unprepared or ill-conceived offerings,[993] and should be permitted to limit offerings on their platforms to issuers that are "crowdfund-ready."[994] Commenters drew a distinction between the permissibility of applying internal screening standards to limited offerings on the platform versus the prohibition on providing investment advice or recommendations.[995] Some commenters suggested that having a disclaimer that "curation" (or limiting offerings on a platform) does not constitute a recommendation on the advisability of any investment displayed on the platform;[996] or that the funding portal does not advertise or make statements that the offerings listed on its platform are safer or better investments than those listed on other platforms,[997] would mitigate regulatory concerns. Some commenters also suggested that the criteria used to limit offerings should be clearly displayed on a funding portal's platform.[998]

In addition, some commenters pointed to a tension in the statute under which a funding portal is potentially subject to liability for material misstatements and omissions in the issuer's offering materials but, at the same time, may be limited in its ability to deny access to its platform.[999] These commenters argued that it was not equitable for a funding portal to have such liability if it cannot determine whether and under what circumstances to permit an issuer or offering access to its platform.

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993 *See* EMKF Letter.

994 *See* SBEC Letter.

995 *See, e.g.,* Angel 1 Letter ("Forcing portals to become the equivalent of common carriers that have to take every offering, no matter how foolish, will make crowdfunding more likely to fail."); Consumer Federation Letter; Saunders Letter.

996 *See, e.g.,* EarlyShares Letter; EMKF Letter; SBA Office of Advocacy Letter.

997 *See* Milken Institute Letter.

998 *See, e.g.,* ABA Letter; CFIRA Letter 1.

999 *See, e.g.,* CrowdCheck 2 Letter; Milken Institute Letter; RocketHub Letter.

(3) Final Rules

In view of the comments, and upon further consideration, we are modifying Rule 402(b)(1) to expressly provide that a funding portal may, consistent with the prohibitions under Exchange Act Section 3(a)(80) (including the prohibition against offering investment advice or recommendations in Section 3(a)(80)(A)), determine whether and under what terms to allow an issuer to offer and sell securities in reliance on Securities Act Section 4(a)(6) through its platform.[1000]

We agree with commenters that the ability of a funding portal to determine which issuers may use its platform is important for the protection of investors, as well as to the viability of the funding portal industry, and thus the crowdfunding market. We acknowledge the concerns raised by commenters that the proposed rules could otherwise have unduly restricted a funding portal's ability to limit offerings conducted on its platform, and we are modifying the safe harbor contained in Rule 402(b)(1) to address these concerns. Specifically, we are revising Rule 402(b)(1) to read that a funding portal may "[d]etermine whether and under what terms to allow an issuer to offer and sell securities in reliance on Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)) through its platform, provided that the funding portal otherwise complies with Regulation Crowdfunding (§§ 227.100 *et seq*.)." The new language is designed to make it clear that a funding portal may exercise its discretion, subject to the prohibition in the statute on providing investment advice or recommendations, to limit the offerings and issuers that it allows

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[1000] *See also* Rule 402(b) (limiting permissible activities to those consistent with the prohibitions under Exchange Act Section 3(a)(80)). The discretion a funding portal has to limit offerings on its platform is in addition to the requirement under Rule 301 to deny access, and cancel offerings, based on fraud and investor protection concerns.

on its platform under the safe harbor, as long as it complies with all other provisions of Regulation Crowdfunding.

In making this change, we recognize that the activities in which a funding portal may engage are, by definition, far more limited than the activities in which a registered broker-dealer may engage. At the same time, we believe that the JOBS Act established an important role for intermediaries, both broker-dealers and funding portals, to play in crowdfunding offerings. While we are providing funding portals with broad discretion to determine whether and under what circumstances to allow an issuer to offer and sell securities through its platform in reliance on Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)), a funding portal must comply with all applicable provisions of Regulation Crowdfunding, including the prohibition on providing investment advice or recommendations. In this regard and as more fully discussed below, among other things, a funding portal cannot advertise, make statements or otherwise represent that the offerings listed on its platform are safer or better investments than those listed on other platforms. Given this statutory restriction, we are not, as some commenters suggested, requiring a funding portal to provide a disclaimer stating that limiting the offerings on its platform does not constitute investment advice or a recommendation, nor are we requiring that its criteria for limiting offerings on its platform be publicly displayed. We do not believe that requiring a funding portal to display its criteria for limiting offerings on its platform will add significant investor protection. While a funding portal may decide to make such criteria public, we caution that a funding portal must avoid any appearance that it is giving investment advice or recommendations or that the funding portal believes its offerings are investment worthy.

b. Highlighting Issuers and Offerings

(1) Proposed Rule

Proposed Rule 402(b)(2) would permit a funding portal to apply objective criteria to highlight offerings on the funding portal's platform where: (i) the criteria are reasonably designed to highlight a broad selection of issuers offering securities through the funding portal's platform, are applied consistently to all issuers and offerings and are clearly displayed on the funding portal's platform; (ii) the criteria may include, among other things, the type of securities being offered (for example, common stock, preferred stock or debt securities); the geographic location of the issuer; the industry or business segment of the issuer; the number or amount of investment commitments made, progress in meeting the issuer's target offering amount or, if applicable, the maximum offering amount; and the minimum or maximum investment amount; *provided* that a funding portal may not highlight an issuer or offering based on the advisability of investing in the issuer or its offering; and (iii) the funding portal does not receive special or additional compensations for highlighting one or more issuers or offerings on its platform.

(2) Comments on Proposed Rule

Several commenters suggested additional criteria for the safe harbor, including for example: (i) how long the issuer has been operational or profitable;[1001] (ii) historical and projected revenue and earnings before interest, taxes, depreciation and amortization (EBITDA);[1002] (iii) the size of the issuer's management team;[1003] (iv) relevant experience and length of experience of the issuer's management;[1004] (v) the type of corporate structure of the issuer;[1005] (vi) the stage and

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1001 *See, e.g.,* CFIRA Letter 1; CFIRA Letter 2.

1002 *Id*.

1003 *Id*.

1004 *See, e.g.,* CFIRA Letter 2.

operating history of the issuer;[1006] (vii) valuation methodology;[1007] (viii) results of securities and background checks;[1008] (ix) "trending";[1009] and (x) most money raised, soonest offering to close, most money invested, least money invested, or on a purely random basis (so long as none of the bases are value-driven – that is, which investment is a safer or better investment).[1010] Another commenter questioned whether, under the safe harbor, funding portals would be permitted to highlight offerings based on their discretion or the use of metrics, such as topic, media coverage, or momentum.[1011] However, another commenter suggested that a funding portal should not have discretion regarding which objective criteria it can use to highlight issuers or offerings because it may result in the portal implicitly recommending securities.[1012] This commenter suggested that the Commission should create a specific list of acceptable objective criteria that a funding portal may apply.[1013]

1005 *See* RocketHub Letter.

1006 *Id*.

1007 *Id*.

1008 *Id*.

1009 *See* Seyfarth Letter.

1010 *See* ASSOB Letter.

1011 *See* RocketHub Letter.

1012 *See* Commonwealth of Massachusetts Letter; *c.f.* ABA Letter (requesting Commission guidance that a portal engaging in activities covered by the safe harbor will not trigger the application of the Investment Advisers Act).

1013 *See* Commonwealth of Massachusetts Letter. *See also* ABA Letter (requesting explicit Commission guidance as to permissible criteria).

Several commenters stated that the criteria used to highlight offerings should be clearly displayed on the platform.[1014] However, one commenter stated that algorithms should not be required to be disclosed on the platform.[1015]

Several commenters suggested that the safe harbor should include the ability of a funding portal to provide mechanisms by which investors can rate an issuer or an offering, which then could be highlighted on the platform.[1016] However, one of these commenters stated that any such rating must be mathematical rather than value-driven or it would amount to "enticement."[1017]

(3) Final Rules

After considering the comments, we are adopting Rule 402(b)(2) as proposed. Specifically, Rule 402(b)(2) allows a funding portal to highlight particular issuers or offerings of securities made in reliance on Section 4(a)(6) on its platform based on objective criteria where the criteria are reasonably designed to highlight a broad selection of issuers offering securities through the funding portal's platform, are applied consistently to all issuers and offerings and are clearly displayed on the funding portal's platform. Consistent with the proposal, the final rule specifies in subparagraph (b)(2)(ii) that objective criteria may include, for example: the type of securities being offered (*e.g.*, common stock, preferred stock or debt securities); the geographic location of the issuer; the industry or business segment of the issuer; the number or amount of investment commitments made; the progress in meeting the target offering amount or, if applicable, the maximum offering amount; and the minimum or maximum investment amount.

1014 *See, e.g.*, ABA Letter; CFIRA Letter 1.

1015 *See* Joinvestor Letter.

1016 *See, e.g.*, ASSOB Letter; CFIRA Letter 1; Joinvestor Letter.

1017 *See* ASSOB Letter.

It is important to note that the criteria must be reasonably designed to highlight a broad selection of issuers and offerings, so as not to recommend or implicitly endorse one issuer or offering over another, and must be applied consistently to all potential issuers and offerings.[1018] This highlighting of issuers or offerings that have been admitted to a funding portal's platform can, depending on relevant facts and circumstances, involve providing investment advice that violates the prohibition on a funding portal providing such advice. To that end, the rule provides a safe harbor only when a funding portal is using objective criteria and such criteria are clearly displayed on its platform to inform investors why certain issuers or offerings are being highlighted.[1019] To reiterate, a funding portal may not highlight an issuer or offering based on the advisability of investing in the issuer or offering or give the impression that the funding portal is providing an implicit (or explicit) recommendation on whether to invest in the issuer or offering.

To help prevent conflicts of interest and incentives for funding portals to favor certain issuers over others, the final rule also prohibits a funding portal from receiving any special or additional compensation for highlighting (or offering to highlight) one or more issuers or offerings on its platform.[1020]

Although some commenters suggested that we include additional criteria in subparagraph (b)(2)(ii), we emphasize that the rule does not establish an exclusive list. The listed criteria are intended as examples, and the safe harbor is non-exclusive. Crowdfunding is a new and evolving market, and we believe that providing principles in the safe harbor by which a funding portal can highlight offerings on its platform will provide it with the flexibility to adapt to the crowdfunding

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1018 *See* Rule 402(b)(2) and (b)(2)(i).

1019 *Id.*

1020 *See* Rule 402(b)(2)(iii) of Regulation Crowdfunding. This rule prohibits paid placements of the kind suggested by one commenter. *See* Earlyshares Letter.

market as it develops while maintaining investor protection. In this regard, the examples listed in Rule 402(b)(2)(ii) are intended to provide guidance to funding portals as they develop their platform and related tools.

Although we are not including additional criteria in Rule 402(b)(2)(ii) at this time, we note that certain of the suggested highlighting criteria are covered by the criteria listed in the rule, such as the issuer's industry; the type of securities being offered; and the geographic location of the issuer's business. Others, while not listed in the final rule, we believe are based on objective criteria, such as the amount of money being raised or size of the offering; soonest offering to close; most or least money invested; how long the issuer has been operational or profitable; the size of the management team of the issuer; the stage and operating history of the issuer; valuation methodology; "trending"; earnings before interest, taxes, depreciation and amortization (EBITDA); and highlighting on a purely random basis. However, we caution that a funding portal must be cognizant not to present highlighted issuers in a manner that, directly or implicitly, results in the provision of investment advice or recommendations.[1021]

c. Providing Search Functions

(1) Proposed Rule

Proposed Rule 402(b)(3) would permit a funding portal to provide search functions or other tools that investors can use to search, sort, or categorize the offerings available through the funding portal's platform according to objective criteria where: (i) the objective criteria may include, among other things, the type of securities being offered (for example, common stock, preferred stock or debt securities); the geographic location of the issuer; the industry or business

[1021] For example, a funding portal may provide the EBITDA of an issuer but it cannot insinuate or state on its platform that the EBITDA corresponds to the advisability of investing in an issuer.

segment of the issuer; the number or amount of investment commitments made, progress in meeting the issuer's target offering amount or, if applicable, the maximum offering amount; and the minimum or maximum investment amount; and (ii) the objective criteria may not include, among other things, the advisability of investing in the issuer or its offering, or an assessment of any characteristic of the issuer, its business plan, its key management or risks associated with an investment.

(2) Comments on Proposed Rule

Several commenters suggested that the safe harbor be broadened to include additional criteria.[1022] One commenter suggested that funding portals should be permitted to sort offerings based on an algorithmic score that takes into account any objective numerical data that is reasonably likely to correlate to successful investments, such as numeric ratings by accredited and unaccredited investors, number of investment commitments weighted by investor portfolio valuation, and number of page views.[1023] Another commenter stated that the use of the word "assessment" in the proposed safe harbor[1024] is inappropriately vague when applied to technology, as it could effectively prohibit the use of any computational sorting algorithm using objective searching and sorting criteria. This commenter suggested that the word "assessment" be substituted with the word "opinion," and also that the term "objective criteria" be removed so that the safe harbor would prohibit the use of *subjective* criteria – such as the advisability of investing or an opinion of any characteristic of the issuer, its business plan, its key management or risks

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1022 *See, e.g.*, EMKF Letter; EquityNet Letter.

1023 *See* EMKF Letter.

1024 Rule 402(b)(3)(ii) states in part that the "objective criteria may not include . . . an assessment of any characteristic of the issuer, its business plan, its key management or risks . . . ."

associated with an investment – "generated exclusively by the portal," excepting instances of peer review and feedback generated by users.[1025]

(3) Final Rules

After considering comments, we are adopting Rule 402(b)(3) substantially as proposed. The final rule permits a funding portal to provide search functions or other tools on its platform that users could use to search, sort or categorize available offerings according to objective criteria.[1026] The final rule also permits search functions that, for example, will allow an investor to sort through offerings based on a combination of different criteria, such as by the percentage of the target offering amount that has been met, geographic proximity to the investor and number of days remaining before the closing date of an offering.[1027] However, the final rule makes clear that the search criteria may not include the advisability of investing in the issuer or its offering, or an assessment of any characteristic of the issuer, its business plan, its management or risks associated with an investment. In this regard, we are making minor changes from proposed Rule 402(b)(3)(i) and (ii) by deleting the word "objective" in the final rules because the term is redundant to the requirement in Rule 402(b)(3) that the criteria be "objective." Further, we are persuaded by one commenter's observation that the use of the word objective in the subparts could be

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1025 *See* EquityNet Letter (noting that "[a]llowing investors the ability to sort through each other's comments or opinions becomes an integral part of any site where commenting is allowed on products" and that "[b]ecause sorting comments would require a technological assessment of subjective data, we believe an explicit carve out in the safe harbor provisions is necessary").

1026 *See* Rule 402(b)(3) Regulation Crowdfunding. *See also* 158 CONG. REC. 2231 (daily ed. Mar. 29, 2012) (statement of Sen. Scott Brown) ("Funding portals should be allowed to organize and sort information based on certain criteria. This will make it easier for individuals to find the types of companies in which they can potentially invest. This type of capability – commonly referred to as curation – should not constitute investment advice.").

1027 *See* Rule 402(b)(3) of Regulation Crowdfunding. Rule 402(b)(3)(i) provides examples of search criteria that are consistent with those listed in the Rule 402(b)(2)(ii) safe harbor for highlighting issuers and offerings.

misleading.[1028] The new sentence structure also makes Rule 402(b)(3) consistent with Rule 402(b)(2), which we believe provides additional clarity and consistency for funding portals when complying with the rules.

Rule 402(b)(3) does not preclude the use of computational sorting algorithms using objective searching and sorting criteria.[1029] However, a funding portal must take care not to indicate that the platform's search results or tools, directly or indirectly, correlate to successful investments. Likewise, we believe that the more particular, biased or weighted a funding portal's algorithm or assessment is, the less likely the criteria as a whole will be objective. However, this does not preclude a funding portal from permitting investors with access to its communication channels from rating issuers or offerings (*e.g.*, a star rating) on its platform or searching such ratings, as long as a funding portal (including its associated persons, such as its employees) does not participate in the rating process.[1030]

d. Providing Communication Channels

(1) Proposed Rule

Proposed Rule 402(b)(4) would address the terms under which a funding portal could provide communication channels by which investors can communicate with one another and with representatives of the issuer through the funding portal's platform about offerings conducted through the platform, as required by Rule 303(c). Under the terms of Rule 402(b)(4) as proposed,

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1028 *See* EquityNet Letter. However, we do not agree with the commenter's assertion that using the word "assessment" in Rule 402(b)(3) equates to a prohibition on the use of computational sorting algorithms using objective searching and sorting criteria because, in this context, assessment is used to refer to subjective criteria.

1029 In response to one commenter's suggestion that a funding portal should be permitted to use algorithmic scores, the final rule does not preclude the use of algorithms as long as the criteria used by the algorithm are objective. *See* EMKF Letter. Thus, a "score" based on an algorithm may be used as long as it does not involve subjective criteria.

1030 *See* Rule 402(b)(4)(i).

the safe harbor would apply so long as the funding portal (and its associated persons): (i) does not participate in these communications, other than to establish guidelines for communication and remove abusive or potentially fraudulent communications; (ii) permits public access to view the discussions made in the communication channels; (iii) restricts posting of comments in the communication channels to those persons who have opened an account on its platform; and (iv) requires that any person posting a comment in the communication channels clearly disclose with each posting whether he or she is a founder or an employee of an issuer engaging in promotional activities on behalf of the issuer, or is otherwise compensated, whether in the past or prospectively, to promote an issuer's offering.

(2) Comments on Proposed Rule

Several commenters supported permitting a funding portal to provide communication channels on its platform through which investors can make comments, rate issuers and provide other feedback, and through which issuers can respond to investor comments.[1031] One of these commenters stated that these capabilities could enable a funding portal to share with investors information related to issuers, capital raised by an issuer, crowd investing, or the crowd-based rating of specific issuers.[1032] Another commenter suggested that funding portals allow investors to assign a quantifiable indicator to each other's comments, so that users can search out the best and worst of the comments and issuers have a chance to respond to investor comments in an open

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1031 *See, e.g.*, CFIRA Letter 1; EquityNet Letter; Milken Institute Letter.

1032 *See* Milken Institute Letter.

forum.[1033] One commenter recommended that permission to rate issuers or offerings should only be given to investors who actually invested in or committed to invest in the offering.[1034]

(3) Final Rules

We are adopting, as proposed, Rule 402(b)(4) to address the terms under which a funding portal can provide communication channels by which investors can communicate with one another and with representatives of the issuer through the funding portal's platform about offerings conducted through the platform, as required by Rule 303(c).[1035] The safe harbor specifies that a funding portal (including its associated persons, such as its employees) may not participate in these communications, other than to establish guidelines about communication and to remove abusive or potentially fraudulent communications. Under Rule 402(b)(4), a funding portal must make communication channels available to the general public and restrict the posting of comments on those channels to those who have accounts on the funding portal's platform. In addition, the funding portal must require each person posting comments to disclose clearly with each posting in the channel whether he or she is a founder or an employee of an issuer engaging in promotional activities on behalf of the issuer, or is otherwise compensated or will receive any compensation for promoting an issuer.[1036]

We agree with commenters that investors should be permitted to communicate with one other, and with representatives of the issuer, over communication channels on the platform

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1033 *See* EquityNet Letter.

1034 *See* CFIRA Letter 1.

1035 *See* Section II.C.5.b(3) for a discussion of Rule 303(c).

1036 *See* Rule 402(b)(4)(iv).

provided by the funding portal.[1037] The communication channel is meant to strengthen and foster the ability of the crowd to communicate. We believe that the capabilities within the communication channel will develop and evolve over time. For example, as noted above, a communication channel may permit investors to rate or comment on an issuer or offering, or to assign quantifiable indicators to one other's comments. Also, a funding portal must make communication channels available for viewing by the general public, and permit anyone who has opened an account on its platform to post comments on the channel.[1038] As we stated in the Proposing Release, requiring investors to have accounts with the funding portal before posting a comment should provide a measure of control over these communications that could aid in promoting accountability for comments made and help ensure that interested persons, such as those associated with the issuer or receiving compensation to promote the issuer, are properly identified.

We reiterate that while a funding portal must provide for a communication channel and may develop certain features or tools as a part of that channel (such as a crowd-based rating system), a funding portal (including its associated persons, such as its employees) may not engage or participate in such communications.[1039] In addition, a funding portal should consider whether the tools or features of the communication channels it develops and the guidelines it establishes for the channel would constitute the funding portal providing impermissible investment advice or recommendations. For example, the funding portal may not establish a guideline that permits a person to rate an offering only if the person provides a positive rating, or otherwise incentivizes

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[1037] As discussed in Section II.C.5, an issuer, its agents and promoters must identify themselves in all communications through the communication channel.

[1038] *See* Rule 402(b)(4)(i) and (ii).

[1039] *See* Rule 402(b)(4)(i). *See also* Rule 303(c).

persons to give positive ratings. However, contrary to what one commenter suggested, we do not believe a funding portal may limit the rating capability to those account holders who have made investment commitments to the relevant offering.[1040] We believe that limiting ratings capability to persons that invest in an offering is likely to skew the ratings, and therefore, we would view such a limitation as inappropriate. Further, such a limitation could prevent persons with relevant and important information about the investment from contributing their views to the crowd.

e. Advising Issuers

(1) Proposed Rule

Proposed Rule 402(b)(5) would permit a funding portal to advise an issuer about the structure or content of the issuer's offering, including assisting the issuer in preparing offering documentation.

(2) Final Rules

We did not receive any comments that specifically addressed the ability of a funding portal to advise issuers and are adopting Rule 402(b)(5) as proposed. The rule permits a funding portal to advise an issuer about the structure or content of the issuer's offering, including preparing offering documentation. We believe funding portals will be in a position to provide experience and assistance to issuers relatively efficiently, and should be able to leverage their expertise to increase the viability of crowdfunding.

We believe that funding portals, as well as broker-dealers, should be permitted to provide certain services to issuers to facilitate the offer and sale of securities in reliance on Section 4(a)(6). Without these services, crowdfunding as a method to raise capital might not be viable. Rule 404(b)(5) permits funding portals to advise an issuer about the structure and content of the issuer's

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[1040] *See* CFIRA Letter 1.

offering in a number of ways. A funding portal can, for example, provide pre-drafted templates or forms for an issuer to use in its offering that will help it comply with its proposed disclosure obligations. Other examples of permissible assistance can include advice about the types of securities the issuer can offer, the terms of those securities and the procedures and regulations associated with crowdfunding.

f. Paying for Referrals

(1) Proposed Rule

Proposed Rule 402(b)(6) would permit a funding portal to compensate a third party for referring a person to the funding portal, so long as the third party does not provide the funding portal with personally identifiable information of any investor and the compensation, other than that paid to a registered broker or dealer, is not based, directly or indirectly, on the purchase or sale of a security in reliance on Section 4(a)(6) of the Securities Act offered on or through the funding portal's platform.

(2) Comment on Proposed Rule

One commenter requested clarification as to: (i) whether and when compensation paid to a non-broker-dealer will be deemed improperly based on the purchase or sale of a security; (ii) whether a funding portal may pay a registered broker-dealer a referral fee without a formal agreement; and (iii) whether a funding portal may charge issuers fees based on the success of the offering.[1041]

(3) Final Rules

We are adopting Rule 402(b)(6) as proposed. Rule 402(b)(6) permits a funding portal to compensate a third party for referring a person to the funding portal if the third party does not

[1041] *See* ABA Letter.

provide the funding portal with personally identifiable information about any investor and the compensation, other than that paid to a registered broker or dealer, is not based, directly or indirectly, on the purchase or sale of a security in reliance on Section 4(a)(6) of the Securities Act offered on or through the funding portal's platform. We believe the safe harbor in this regard addresses the prohibition in Rule 305 against an intermediary compensating any person for providing the intermediary with the personally identifiable information of any investor in securities offered and sold in reliance on Section 4(a)(6). We also believe that Rule 402(b)(6)'s prohibition on funding portals paying transaction-based compensation to third parties, other than that paid to a registered broker or dealer, will help to minimize the incentive for high-pressure sales tactics and other abusive practices in this area. One commenter requested additional guidance as to what types of compensation would equate to compensation based on the offer or sale of a security.[1042] The Commission and courts have interpreted the definition of transaction-based compensation broadly,[1043] and whether compensation is transaction-based is a facts and circumstances determination. Thus, we do not believe that additional guidance is necessary or appropriate in this context.

In response to a commenter's inquiry, a funding portal may not pay a registered broker-dealer a referral fee without a written agreement under the safe harbor. Such an arrangement would be covered by Rule 402(b)(7), which is discussed below.

1042 *Id.*

1043 *See*, *e.g.*, Applicability of Broker-Dealer Registration to Banks, Exchange Act Rel. No. 20,357 at n.14 (Nov. 8, 1983).

g. Compensation Arrangements with Registered Broker-Dealers

(1) Proposed Rule

Proposed Rule 402(b)(7) would permit a funding portal to pay or offer to pay any compensation to a registered broker or dealer for services in connection with the offer or sale of securities by the funding portal in reliance on Section 4(a)(6) of the Act, provided that: (i) such services are provided pursuant to a written agreement between the funding portal and the registered broker or dealer; (ii) such services and compensation are permitted under Regulation Crowdfunding and are not otherwise prohibited under Rule 305; and (iii) such compensation complies with and is not prohibited by the rules of any registered national securities association of which the funding portal is required to be a member.

Proposed Rule 402(b)(8) would permit a funding portal to receive any compensation from a registered broker or dealer for services provided by the funding portal in connection with the offer or sale of securities by the funding portal in reliance on Section 4(a)(6) of the Act, provided that: (i) such services are provided pursuant to a written agreement between the funding portal and the registered broker or dealer; (ii) such compensation is permitted under Regulation Crowdfunding; and (iii) such compensation complies with and is not prohibited by the rules of any registered national securities association of which the funding portal is required to be a member.

(2) Comments on Proposed Rule

Several commenters expressed concerns about the permitted relationships between funding portals and broker-dealers.[1044] One of these commenters stated that the proposed safe harbor is "overly broad" and creates "unmanageable conflicts between funding portals and broker dealers,"

[1044] *See, e.g.*, Commonwealth of Massachusetts Letter; RocketHub Letter.

and suggested the Commission prevent these conflicts by prohibiting funding portals from paying broker-dealers any type of compensation in connection with the offer or sale of securities under the crowdfunding exemption.[1045] Another of these commenters suggested that the Commission require relationships between funding portals and brokers to be arms-length and, if they are not, require that the funding portal activity be operated by the broker-dealer entity.[1046]

(3) Final Rules

We are adopting Rule 402(b)(7) generally as proposed, but with minor modifications for clarity and consistency. Rule 402(b)(7) specifies that a funding portal may pay or offer to pay compensation to a registered broker or dealer for services, including for referring a person to the funding portal, in connection with the offer or sale of securities by the funding portal in reliance on Section 4(a)(6) of the Securities Act, provided that (i) such services are provided pursuant to a written agreement between the funding portal and the registered broker or dealer; (ii) such compensation is permitted under Regulation Crowdfunding; and (iii) such compensation complies with the rules of any registered national securities association of which the funding portal is a member. As discussed above, proposed Rule 402(b)(7) did not contain a reference to "referrals," while proposed Rule 402(b)(6) included the language "for referring a person to the funding portal." We have added a reference to "referrals pursuant to [Rule 402](b)(7)" to make clear that all payment arrangements with a broker-dealer, including paying a broker-dealer for referrals as permitted under subparagraph (b)(6), must be in writing.

Proposed Rule 402(b)(7)(ii) had also stated that "such compensation is permitted under this part and is not otherwise prohibited under § 227.305"; and subparagraph (b)(7)(iii) stated

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1045 *See* Commonwealth of Massachusetts Letter.

1046 *See* RocketHub Letter (expressing concern over broker-dealers creating entities that would register as funding portals so as to evade FINRA oversight as a broker-dealer).

"such compensation complies with and is not prohibited by-the rules of any registered national securities association of which the funding portal is required to be a member." We are deleting the phrases "and is not otherwise prohibited under § 227.305" and "and is not prohibited by" to make the language in Rule 402(b)(7) and Rule 402(b)(8) consistent, and because the phrases are redundant. Also, we are deleting the phrase "required to be a member" and replacing it with "is a member" in recognition of the fact that additional national securities associations may exist in the future and that a funding portal would only have to be a member of one such association.

Consistent with Rule 402(b)(7), a funding portal may, for example, pay a broker-dealer for certain services, such as information technology services, qualified third party services or referral services, pursuant to a written agreement. Each party to this type of arrangement will need to comply with all applicable regulations, including the rules of the registered national securities association of which it is a member.

Similarly, we are adopting Rule 402(b)(8) as proposed with minor modifications. Rule 402(b)(8) permits a funding portal to provide services to, and receive compensation from, a registered broker-dealer in connection with the funding portal's offer or sale of securities in reliance on Section 4(a)(6), provided that: (i) such services are provided pursuant to a written agreement between the funding portal and the registered broker or dealer; (ii) such compensation is permitted under Regulation Crowdfunding; and (iii) such compensation complies with the rules of any registered national securities association of which the funding portal is a member. The proposed rules had stated that "such compensation complies with and is not prohibited by the rules of any registered national securities association of which the funding portal is required to be a member." For the reasons discussed above with regard to Rule 402(b)(7)(ii), we are deleting the

phrase "and is not prohibited" because it is redundant and deleting the phrase "required to be a member" and replacing it with "is a member."

Pursuant to Rule 402(b)(8), a funding portal may receive compensation, including transaction-based compensation, from a broker-dealer for providing referrals to that broker-dealer relating to an offering made pursuant to Section 4(a)(6). It is important to emphasize that the safe harbor does not permit a funding portal to receive transaction-based compensation for referrals of investors in other types of offerings, such as Rule 506 offerings, that are effected by a registered broker-dealer.[1047] Further, these arrangements must be compliant with Rule 305, which prohibits, with certain exceptions, an intermediary from compensating any person for providing the intermediary with the personally identifiable information of any investor.[1048] As we stated in the Proposing Release, the safe harbor is intended to facilitate intermediaries' cooperation with each other and promote the use of the Section 4(a)(6) exemption to raise capital, while maintaining a written record of compensation payments.

We disagree with the commenter who suggested that Rules 402(b)(7) and (8) create an unmanageable conflict between funding portals and broker-dealers.[1049] We believe that any potential conflict of interest between broker-dealers and funding portals as a result of compensation arrangements is mitigated due to the fact that both entities are registered with the Commission and members of FINRA and because permissible activities under Rule 402(b)(7) and (8) are limited by Regulation Crowdfunding. We also are not prohibiting a registered broker-dealer and a registered funding portal from being affiliated, nor are we requiring that any

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[1047] Receipt of transaction-based compensation in connection with such referrals can cause a funding portal to be a broker required to register with us under Exchange Act Section 15(a)(1) (15 U.S.C. 78*o*(a)(1)).

[1048] *See* Section II.C.7 (discussing Rule 305).

[1049] *See* Commonwealth of Massachusetts Letter.

crowdfunding operation be performed by the registered broker-dealer in such an affiliation.[1050] Because funding portals and broker-dealers are each registered with the Commission and required to be members of a registered national securities association with the attendant rules and oversight, we believe concerns about conflicts of interests among affiliated funding portals and broker-dealers are sufficiently mitigated by this regulatory framework.

While a commenter questioned whether a funding portal may pay introducing brokers a fee for referring persons to the funding portal without a formal written arrangement,[1051] we emphasize that Rule 402(b)(7) requires all such arrangements to be in writing.

h. Advertising

(1) Proposed Rule

Proposed Rule 402(b)(9) would permit a funding portal to advertise the existence of the funding portal and identify one or more issuers or offerings available on the portal on the basis of objective criteria, as long as: (i) the criteria are reasonably designed to identify a broad selection of issuers offering securities through the funding portal's platform and are applied consistently to all potential issuers and offerings; (ii) the criteria may include, among other things, the type of securities being offered (for example, common stock, preferred stock or debt securities); the geographic location of the issuer; the industry or business segment of the issuer; the expressed interest by investors, as measured by number or amount of investment commitments made, progress in meeting the issuer's target offering amount or, if applicable, the maximum offering amount; and the minimum or maximum investment amount; and (iii) the funding portal does not receive special or additional compensation for identifying the issuer or offering in this manner.

1050 *See* RocketHub Letter (expressing concern over broker-dealers creating entities that would register as funding portals, so as to evade FINRA oversight as a broker-dealer).

1051 *See* ABA Letter.

(2) Comments on Proposed Rule

Several commenters supported the proposed safe harbor on funding portal advertising.[1052] However, commenters were divided on whether funding portals should be permitted to advertise current offerings and issuers in their advertisements. One commenter was supportive of allowing funding portals to "advertise more generally, as well as highlight ongoing offerings through various communication channels."[1053] The same commenter stated that a portal's decision to feature or highlight issues available should not be viewed by the Commission as investment advice, a recommendation, or a solicitation.[1054] This commenter nonetheless cautioned that "[p]ortals should be barred from language that implicates the level of risk involved in the investment or the overall quality of the investment opportunity" as well as "from soliciting investments for any specific campaign by providing offering details outside of the Portal itself."[1055] Another commentator expressed opposition to "a limitation on the funding portal to only advertise its past offerings," stating that such a limitation "would be overly restrictive."[1056]

In contrast, one commenter stated that, while funding portals should be allowed to advertise, funding portals should not be able to display specific issuers in their advertising materials.[1057] This commenter stated that "[t]he concern with displaying individual issuers is that investors will interpret this as a recommendation and endorsement of the issuer."[1058] The commenter noted that the prohibition on providing recommendations can be easily circumvented

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1052 *See, e.g.*, CFIRA Letter 1; Commonwealth of Massachusetts Letter; ABA Letter.

1053 *See* RocketHub Letter.

1054 *Id*.

1055 *Id*.

1056 *See* CFIRA Letter 1.

1057 *See* Commonwealth of Massachusetts Letter.

1058 *Id*.

by manipulating otherwise seemingly objective criteria, and that funding portals could advertise offerings based on certain criteria, such as high target offerings, that may generate more money for the funding portal (*i.e.*, a funding portal can mask self-interest by using objective criteria).[1059] This same commenter suggested that the Commission could allow descriptions of the portals themselves and the specific business segments featured on their websites, without mentioning specific issuers currently registered with the portal.[1060]

One commenter suggested the Commission clarify that it would be inappropriate for a funding portal to send out soliciting e-mails recommending investment in particular companies to investors who have signed up with that portal.[1061] Another commenter stated that a funding portal should not be permitted to advertise or otherwise make statements that offerings listed are somehow safer or better than other platforms.[1062]

(3) Final Rules

We are adopting Rule 402(b)(9) as proposed. Rule 402(b)(9) permits a funding portal to advertise its existence and identify one or more issuers or offerings available on the portal on the basis of objective criteria, as long as: (i) the criteria are reasonably designed to identify a broad selection of issuers offering securities through the funding portal's platform and are applied consistently to all potential issuers and offerings; (ii) the criteria may include, among other things, the type of securities being offered (for example, common stock, preferred stock or debt securities); the geographic location of the issuer; the industry or business segment of the issuer; the expressed interest by investors, as measured by number or amount of investment commitments

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1059 *Id*.

1060 *Id*.

1061 *See* ABA Letter.

1062 *See* Milken Institute Letter.

made, progress in meeting the issuer's target offering amount or, if applicable, the maximum offering amount; and the minimum or maximum investment amount; and (iii) the funding portal does not receive special or additional compensation for identifying the issuer or offering in this manner. However, a funding portal may not base its decision as to which issuers to include in its advertisements on whether it has a financial interest in the issuer,, and any advertising may not directly or indirectly favor issuers in which the funding portal has invested or will invest.

After considering the comment letters, we believe that the requirements of the safe harbor, including the requirement for objective criteria designed to result in a broad selection of highlighted issuers or offerings, will result in advertisements that are focused on the funding portal itself, as opposed to recommending a particular offering or offerings.[1063] Funding portals continue to be subject to the statutory prohibition on providing investment advice and recommendations.[1064] An advertisement by a funding portal must not be an implicit (or explicit) recommendation as to whether to invest in the issuer or offering or advice on the advisability of investing in the issuer or offering. Therefore, consistent with the views of one commenter, a funding portal may not advertise in such a way that expresses the funding portal's view that, for example, certain offerings on its platform are of a higher quality, safer or more worthy than others, or that otherwise gives a recommendation.[1065]

We recognize that advertisements can take many varied forms, including non-traditional means, such as blogs, e-mails through social media or other methods. We believe that these types of communications, when made by a funding portal to investors can be a permissible means of

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1063 The safe harbor is limited to identifying one or more issuers. More detailed information about an issuer should be provided on the funding portal's platform.

1064 *See* Exchange Act Section 3(a)(80)(A).

1065 *See* Milken Institute Letter.

advertising within the scope of Rule 402(b)(9). We agree, however, with a commenter's statement that it would be inconsistent with the statutory prohibition on providing investment advice or recommendations for a funding portal to send out soliciting e-mails recommending investments in particular companies as part of its advertising.[1066]

i. Deny Access to Platform

(1) Proposed Rule

Proposed Rule 402(b)(10) would permit a funding portal to deny access to its platform to, or cancel an offering of, an issuer that the funding portal believes may present the potential for fraud or otherwise raises investor protection concerns.

(2) Comments on Proposed Rule

Some commenters asserted that the proposed rules are ambiguous, and that the lack of specificity exposes funding portals to potential liability. The commenters were concerned that the perceived lack of specificity may also lead funding portals to unintentionally violate the ban on providing investment advice with their attempts to mitigate liability.[1067]

(3) Final Rules

We are adopting Rule 402(b)(10) substantially as proposed with modifications to make it consistent with Rule 301(c)(2), which requires an intermediary to deny access if it has a reasonable basis for believing that the issuer or the offering presents the potential for fraud or otherwise raises concerns about investor protection.[1068] In satisfying this requirement, an intermediary must deny access if it reasonably believes that it is unable to adequately or effectively assess the risk of fraud of the issuer or its potential offering. In addition, if an

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1066 *See* ABA Letter.

1067 *See, e.g.*, RocketHub Letter and Seyfarth Letter.

1068 *See* Section II.C.3 discussing the change to Rule 301(c) to include a "reasonable basis" standard.

intermediary becomes aware of information after it has granted access that causes it to reasonably believe that the issuer or the offering presents the potential for fraud or otherwise raises concerns about investor protection, the intermediary must promptly remove the offering from its platform, cancel the offering, and return (or, for funding portals, direct the return of) any funds that have been committed by investors in the offering. Rule 402(b)(10) requires a funding portal to deny access to its platform to, or cancel an offering of an issuer, pursuant to Rule 301(c)(2), if the funding portal has a reasonable basis for believing that the issuer or the offering presents the potential for fraud or otherwise raises concerns.

We changed the standard in Rule 402(b)(10) to a "reasonable basis for believing" – rather than "believes" – to conform the safe harbor to the requirements of Rule 301(c)(2) as adopted. Thus, the standard in Rule 402(b)(10) is consistent with the modifications that we made to the standard in Rule 301(c)(2).[1069] We believe this change also should help to address commenters' concerns about the perceived lack of specificity in the proposed safe harbor by providing an objective "reasonable belief" standard for the required determinations. Under this standard a funding portal may not ignore facts about an issuer that indicate fraud or investor protection concerns such that a reasonable person would have denied access to the platform. At the same time, a funding portal can also feel assured in its decision to deny an issuer access or cancel an offering if it has a reasonable basis for such a determination. We also believe that including a "reasonable basis" standard adds objectivity to a funding portal's determinations regarding which issuers must be denied access to (or removed from) its platform, which is expected to help to address concerns regarding the clarity of the standard under the proposed rule.

[1069] *See* Section II.C.3.

j. Accepting Investor Commitments

(1) Proposed Rule

Proposed Rule 402(b)(11) would permit a funding portal to accept, on behalf of an issuer, an investment commitment for securities offered in reliance on Section 4(a)(6) of the Securities Act by that issuer on the funding portal's platform.

(2) Comments on Proposed Rule

One commenter noted that the statute prohibits funding portals from handling investor funds or securities, and that the proposed rule requiring the use of third-party entities would create additional transaction costs for funding portals.[1070] Another commenter stated that the safe harbor for accepting investor commitments should permit a funding portal to assist issuers in handling a direct registration system (DRS) between issuers and investors.[1071]

(3) Final Rules

We are adopting Rule 402(b)(11) as proposed. Rule 402(b)(11) permits a funding portal, on behalf of an issuer, to accept investment commitments from investors for securities offered in reliance on Section 4(a)(6) by that issuer on the funding portal's platform. We are not broadening the safe harbor to permit funding portals to handle customer funds, as suggested by one commenter. Although we recognize that the requirement to use a third party entity to handle customer funds imposes an additional expense on a funding portal, Exchange Act Section 3(a)(80)(D) explicitly prohibits funding portals from handling customer funds and securities. Similarly, we believe it would be inconsistent with the statute for a funding portal to facilitate a

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1070 *See* Stephenson, *et al*., Letter.

1071 *See* RocketHub (suggesting that a portal should be permitted to provide DRS support to issuers and investors). A DRS allows investors to transfer a security that is registered in the investor's name on the issuer's books, and either the company or its transfer agent holds the security for the investor in book-entry form.

securities registration system for issuers and investors because such activity implicitly requires funding portals to handle customer funds and securities, which is prohibited by the statute. In this regard, we note that the activities that a funding portal is permitted to engage in are limited in scope, and as such are subject to a more limited regulatory scheme as compared to registered broker-dealers.

k. Directing Transmission of Funds

(1) Proposed Rule

Proposed Rule 402(b)(12) would permit a funding portal to direct investors where to transmit funds or remit payment in connection with the purchase of securities offered and sold in reliance on Section 4(a)(6) of the Securities Act.

Proposed Rule 402(b)(13) would permit a funding portal to direct a qualified third party, as required by Rule 303(e), to release proceeds to an issuer upon completion of a crowdfunding offering or to return proceeds to investors in the event an investment commitment or an offering is cancelled.

(2) Final Rules

We did not receive comments on the ability of a funding portal to direct investment funds and are adopting Rules 402(b)(12) and (13) as proposed. Rules 402(b)(12) and (13) provide that a funding portal can fulfill its obligations with respect to the maintenance and transmission of funds and securities, as set forth in Rule 303, without violating the prohibition in Exchange Act Section 3(a)(80)(D). Specifically, a funding portal can direct investors where to transmit funds or remit payment in connection with the purchase of securities offered and sold in reliance on Section

4(a)(6),[1072] and as required by Rule 303(e), a funding portal can direct a qualified third party to release the proceeds of an offering to the issuer upon completion of the offering or to return investor proceeds when an investment commitment or offering is cancelled.[1073]

l. Posting News

In the Proposing Release, we asked whether we should adopt a safe harbor that permits a funding portal to post news, such as market news and news about a particular issuer or industry, on its platform. In response to our request for comment, some commenters stated that the safe harbor should permit funding portals to post third party news related to issuers or offerings on their platform.[1074] One commenter cautioned that objective criteria should be used to ensure, for example, that funding portals are not picking out the most flattering or positive news.[1075] Another commenter suggested that funding portals should be aware of the content of materials posted on their portal and held responsible for inappropriate information that is posted.[1076]

While we believe it is possible for funding portals to post news on their platforms in a manner that would not violate the prohibitions in Exchange Act Section 3(a)(80), we are not including such activities within the safe harbor because we believe the permissibility of posting news should be a facts and circumstances determination. When posting news, funding portals will need to ensure that they do not violate the prohibition on giving investment advice and recommendations. For example, if a funding portal selectively determines which news articles to

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1072 *See* Rule 402(b)(12) of Regulation Crowdfunding.

1073 *See* Rule 402(b)(13) of Regulation Crowdfunding.

1074 *See, e.g.*, CFIRA Letter 1; RoC Letter; StartupValley Letter. *But see* Joinvestor Letter; Wefunder Letter.

1075 *See* CFIRA Letter 1.

1076 *See* RoC Letter.

post or posts only flattering or positive news, then the funding portal is more likely to be giving impermissible investment advice or recommendations.

m. No Presumption and Anti-Fraud Provisions

(1) Proposed Rule

Proposed Rule 402(a) also stated that no presumption shall arise that a funding portal has violated the prohibitions under Section 3(a)(80) of the Exchange Act or Regulation Crowdfunding by reason of the funding portal or its associated persons engaging in activities in connection with the offer or sale of securities in reliance on Section 4(a)(6) of the Securities Act that do not meet the conditions specified in the safe harbor and that the antifraud provisions and all other applicable provisions of the federal securities laws continue to apply to the activities described in the safe harbor.

(2) Final Rules

We did not receive any comments on the proposed "no presumption" and anti-fraud provisions and are adopting Rule 402(a) as proposed. We also reiterate that Rule 402(b) is a non-exclusive safe harbor. Rule 402(a) expressly provides that the failure of a funding portal to meet the conditions of the safe harbor does not give rise to a presumption that the funding portal is in violation of the statutory prohibitions of Exchange Act Section 3(a)(80) or Regulation Crowdfunding.[1077]

Further, the safe harbor under Rule 402 does not prohibit funding portals from engaging third party service providers to assist the funding portal in operating its platform, such as providers of software, website maintenance and development, communication channel

[1077] *See* Rule 402(a) of Regulation Crowdfunding.

applications, recordkeeping systems, and other technology.[1078] However, the funding portal remains responsible for its activities and the operation of its platform and for compliance with Regulation Crowdfunding and other applicable federal securities laws.

4. Compliance

a. Policies and Procedures

(1) Proposed Rule

As proposed, Rule 403(a) would require a funding portal to implement written policies and procedures reasonably designed to achieve compliance with the federal securities laws and the rules and regulations thereunder, relating to its business as a funding portal.[1079]

(2) Comments on the Proposed Rules

One commenter agreed that the Commission should not specify requirements for a funding portal's policies and procedures, while another commenter thought the Commission should provide guidance concerning the policies and procedures.[1080] Another commenter suggested that all changes to a funding portal's policies and procedures should be disclosed within 30 days and publicly announced.[1081] Yet another commenter suggested requiring the SRO to mandate that broker-dealers and funding portals follow the same policies.[1082]

1078 One commenter asked whether funding portals could engage third party service providers consistent with Regulation Crowdfunding. *See* CFIRA Letter 1.

1079 As a condition to exempting funding portals from the requirement to register as a broker or a dealer under Exchange Act Section 15(a)(1) (15 U.S.C. 78*o*(a)(1)), Exchange Act Section 3(h)(1)(C) provides that registered funding portals must comply with such other requirements as the Commission determines appropriate.

1080 *See* ASSOB Letter; Consumer Federation of America ("[The Commission] fails to address at all the areas that should be covered by such policies and procedures, or what a funding portal's responsibilities to monitor compliance would be.").

1081 *See* Joinvestor Letter.

1082 *See* Rockethub Letter.

(3) Final Rules

We are adopting Rule 403(a) as proposed. We believe that the requirement to implement written policies and procedures will provide important investor protections as it will necessitate that funding portals remain aware of the various regulatory requirements to which they are subject and take appropriate steps for complying with such requirements. We recognize, however, that funding portals may have various business models and, therefore, consistent with the views of one commenter, we are not imposing specific requirements for a funding portal's policies and procedures, provided the policies and procedures are reasonably designed to achieve compliance with the federal securities laws and the rules relating to their business as funding portals. Rather, we are providing a funding portal with discretion to establish, implement, maintain and enforce its policies and procedures based on its relevant facts and circumstances.

We note, however, that a funding portal may rely on the representations of others when meeting certain requirements under Regulation Crowdfunding, unless the funding portal has reason to question the reliability of those representations. For example, a funding portal may rely on an issuer's representation to establish a reasonable basis for believing that an issuer seeking to offer and sell securities in reliance on Section 4(a)(6) through its platform complies with the requirements in Securities Act Section 4A(b) and the related requirements in Regulation Crowdfunding, unless the funding portal has reason to question the reliability of that representation.[1083] A funding portal may also rely on an investor's representation to establish a reasonable basis for believing that an investor satisfies the investment limits established by Section 4(a)(6)(B), unless the funding portal has reason to question the reliability of that

[1083] *See* Rule 301(a).

representation.[1084] We believe that when a funding portal relies on the representations of others to form a reasonable basis, the funding portal should have policies and procedures regarding under what circumstances it can reasonably rely on such representations and when additional investigative steps may be appropriate. We further believe that a funding portal's policies and procedures should cover not only permitted activities, but also address prohibited activities. For example, a funding portal should have policies and procedures on the criteria used to limit, highlight and advertise issuers and offerings.

We note one commenter's suggestion that we require funding portals to update their policies and procedures to reflect changes in applicable rules and regulations within a specified time period after the change occurs. However, as explained in the Proposing Release, we believe that the requirement for reasonably designed policies and procedures includes an ongoing obligation for a funding portal to promptly update its policies and procedures if necessary to reflect changes in applicable rules and regulations, a funding portal's business practices, and/or the marketplace.[1085] Finally, in response to one commenter's suggestion that we require SROs to mandate that broker-dealers and funding portals follow the same policies, as noted above, we believe that funding portals should have flexibility to implement policies and procedures suited to their own facts and circumstances. Moreover, we note that any proposed SRO rules relating to policies and procedures of either broker-dealers or funding portals will be subject to the Exchange Act Section 19(b) SRO rule filing process.[1086]

1084 *See* Rule 303(b)(1).

1085 Consistent with our requirements for broker-dealers, we are not requiring that a funding portal's policies and procedures be made public, as suggested by a commenter.

1086 Pursuant to Exchange Act Section 19(b) and Rule 19b-4, SROs are required to file proposed new rules and rule changes with the Commission.

Commission staff expects to review intermediaries' compliance policies and procedures relating to their activities in connection with the offer or sale of securities in reliance on Section 4(a)(6) during the study of the federal crowdfunding exemption that it plans to undertake no later than three years following the effective date of Regulation Crowdfunding.[1087]

b. Anti-Money Laundering

(1) Proposed Rule

Proposed Rule 403(b) would require that funding portals comply with certain AML provisions,[1088] as set forth in Chapter X of Title 31 of the Code of Federal Regulations. The BSA and its implementing regulations establish the basic framework for AML obligations imposed on financial institutions.[1089] The BSA is intended to facilitate the prevention, detection and prosecution of money laundering, terrorist financing and other financial crimes.

Among other things, the BSA and its implementing regulations require a "broker or dealer in securities" (sometimes referred to in the regulations as a "broker-dealer") to: (1) establish and maintain an effective AML program;[1090] (2) establish and maintain a Customer Identification Program;[1091] (3) monitor for and file reports of suspicious activity (SARs);[1092] and (4) comply with requests for information from the Financial Crimes Enforcement Network ("FinCEN").[1093] For purposes of the BSA obligations, a "broker or dealer in securities" is defined as a "broker or dealer in securities, registered or required to be registered with the Securities and Exchange

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1087 *See* Section II.

1088 *See also* Section II.D.2. (discussing proposed Rule 401(b)).

1089 *See* BSA, note 981; 31 CFR Chapter X.

1090 *See* 31 U.S.C. 5318(h). *See also* 31 CFR 1023.210; FINRA Rule 3310.

1091 *See* 31 CFR 1023.220.

1092 *See* 31 CFR 1023.320. *See also* FINRA Rule 3310.

1093 *See* 31 CFR 1010.520.

Commission under the Securities Exchange Act of 1934, except persons who register pursuant to [S]ection 15(b)(11) of the Securities Exchange Act of 1934."[1094] As explained above, Exchange Act Section 3(h) expressly directs the Commission, conditionally or unconditionally, to exempt funding portals from the requirement to register as a broker or dealer under Section 15(a). As such, a funding portal is not a broker "registered or required to be registered" if it registers as a funding portal with the Commission. We proposed that, notwithstanding this exemption from broker registration, under Rule 401(b) a funding portal would be "required to be registered" as a broker or dealer with the Commission under the Exchange Act solely for purposes of Chapter X of Title 31 of the Code of Federal Regulations, thus subjecting funding portals to the AML requirements of Chapter X of Title 31.

(2) Comments on the Proposed Rule

A few commenters generally suggested that since funding portals are prohibited from handling customer funds and securities they should not be required to comply with AML provisions.[1095] Some commenters, however, generally supported requiring funding portals to comply with AML provisions.[1096] One commenter, noting that non-U.S. investors may participate in crowdfunding and use U.S.-based funding portals, requested that the Commission provide advice and suggestions on "how to prevent anti-money laundering."[1097]

1094 *See* 31 CFR 1010.100(h). As noted above, certain FinCEN regulations apply to a "broker-dealer," which is defined as a "person registered or required to be registered as a broker or dealer with the Commission under the Securities Exchange Act of 1934 (15 U.S.C. 77a *et seq*.), except persons who register pursuant to 15 U.S.C. 78*o*(b)(11)." 31 CFR 1023.100(b). Such broker-dealers also would meet the definition of "broker or dealers in securities" above.

1095 *See* PeoplePowerFund Letter; Public Startup 3 Letter; RFPIA Letter; Vann Letter.

1096 *See* RocketHub Letter (stating that it "supports the Commissions [sic] interpretation of the exemption, and believes that AML compliance is necessary"); Berlingeri Letter (supporting funding portal "compliance with existing anti-money laundering provisions and the requirement to report suspicious activity").

1097 *See* Zhang Letter.

(3) Final Rules

Upon further consideration, we have determined not to adopt proposed Rule 403(b). The BSA requirements play a critical role in detecting, preventing, and reporting money laundering and other illicit financing, such as market manipulation and fraud. However, after careful consideration, we believe that AML obligations for funding portals are better addressed outside of the rules that we are currently adopting in this release, and that it would be more appropriate to work with other regulators to develop consistent and effective AML obligations for funding portals.[1098] We note, however, that broker-dealers continue to have their own AML obligations, as do certain other parties involved in transactions conducted pursuant to Section 4(a)(6), such as a bank acting as a qualified third party to hold investor funds.

c. Privacy

(1) Proposed Rule

Section 4A(a)(9) of the Securities Act requires intermediaries to take such steps to protect the privacy of information collected from investors as the Commission shall, by rule, determine appropriate. Proposed Rule 403(c) would implement the requirements of Section 4A(a)(9) by subjecting funding portals to the same privacy rules as those applicable to brokers. Proposed Rule 403(c), therefore, would have required funding portals to comply with Regulation S-P (Privacy of

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1098 FinCEN within the Department of Treasury has primary regulatory responsibility for administering the BSA. We note that FinCEN has included in the Unified Agenda and Regulatory Plan an item that states: "FinCEN…is proposing amendments to the regulatory definitions of 'broker or dealer in securities' under the regulations implementing the Bank Secrecy Act. The proposed changes are intended to expand the current scope of the definitions to include funding portals. In addition, these amendments would require funding portals to implement policies and procedures reasonably designed to achieve compliance with all of the Bank Secrecy Act requirements that are currently applicable to brokers or dealers in securities." *See* Office of Mgmt. & Budget, Exec. Office of the President, Office of Info. & Regulatory Affairs, Amendments of the Definition of Broker or Dealer in Securities, RIN 1506-AB29, *available at* http://www.reginfo.gov/public/do/eAgendaViewRule?pubId=201504&RIN=1506-AB29. In addition, the Commission has adopted its own rules that require broker-dealers to comply with certain requirements of the BSA's implementing regulations, such as books and records requirements. *See* Exchange Act Rule 17a-8. *See also* Section II.D.5.

Consumer Financial Information and Safeguarding Personal Information),[1099] Regulation S-AM (Limitations on Affiliate Marketing),[1100] and Regulation S-ID (Identity Theft Red Flags)[1101] (collectively, the "Privacy Rules").[1102]

Regulation S-P governs the treatment of nonpublic personal information by brokers, among others.[1103] It generally requires a broker to provide notice to investors about its privacy policies and practices; describes the conditions under which a broker may disclose nonpublic personal information about investors to nonaffiliated third parties; and provides a method for investors to prevent a broker from disclosing that information to most nonaffiliated third parties by "opting out" of that disclosure, subject to certain exceptions. Regulation S-AM allows a consumer, in certain limited situations, to block affiliates of covered persons (*i.e.*, brokers, dealers, investment companies and both investment advisers and transfer agents registered with the Commission) from soliciting the consumer based on eligibility information (*i.e.*, certain financial information, such as information about the consumer's transactions or experiences with the covered person) received from the covered person.[1104] Regulation S-ID generally requires brokers to develop and implement a written identity theft prevention program that is designed to detect,

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1099 *See Privacy of Consumer Financial Information (Regulation S–P)*, Release No. 34-42974 (June 22, 2000) [65 FR 40334 (June 29, 2000)].

1100 *See Regulation S–AM: Limitations on Affiliate Marketing*, Release No. 34-60423 (Aug. 4, 2011) [74 FR 40398 (Aug. 11, 2009)].

1101 *See Identity Theft Red Flags Rules*, Release No. 34-69359 (Apr. 10, 2013) [78 FR 23637 (Apr. 19, 2013)] (adopted jointly with the Commodity Futures Trading Commission).

1102 *See* 17 CFR 248.

1103 *See* 17 CFR 248 Subpart A.

1104 *See* 17 CFR 248 Subpart B.

prevent and mitigate identity theft in connection with certain existing accounts or the opening of new accounts.[1105]

(2) Comments and Final Rules

We are adopting Rule 403(c) as proposed, but renumbering it as Rule 403(b).[1106] One commenter opposed Proposed Rule 403(c), which would impose the Privacy Rules on funding portals, stating that in its view, funding portals do not raise privacy concerns.[1107] We disagree. We believe that privacy is a concern as it relates to funding portals given that funding portals will collect and maintain sensitive personal information about the investors using their platforms.

d. Inspections and Examinations

(1) Proposed Rule

Exchange Act Section 3(h)(1)(A) specifies that funding portals must remain subject to our examination authority to, among other things, rely on any exemptions from broker-dealer registration that we impose. Under proposed Rule 403(d) of Regulation Crowdfunding, a funding portal would be required to permit the examination and inspection of all of its business and business operations that relate to its activities as a funding portal, such as its premises, systems, platforms and records, by our representatives and by representatives of the registered national securities association of which it is a member.

1105 *See* 17 CFR 248 Subpart C.

1106 The rule is being renumbered to account for the elimination of the proposed AML provision in proposed Rule 403(b), which is discussed in Section II.D.4.b above.

1107 *See* Public Startup Letter 3.

(2) Comment and Final Rules

We are adopting Rule 403(d) as proposed, but renumbering it as 403(c).[1108] One commenter opposed the Commission's proposed inspections and examinations rules as unnecessary.[1109] As a condition to exempting funding portals from the requirement to register as broker-dealers under Exchange Act Section 15(a)(1), Exchange Act Section 3(h)(1)(A) requires that registered funding portals remain subject to, among other things, our examination authority. We believe that inspections and examinations are an important aspect of our oversight function of funding portals as they will assist us in monitoring the activities of funding portals in light of applicable statutory and regulatory requirements. Therefore, we are adopting Rule 403(c) to implement the statute and retain examination authority over funding portals.

5. Records to be Created and Maintained by Funding Portals

a. Proposed Rule

As proposed, Rule 404(a) would require funding portals to make and preserve certain records for five years, with the records retained in a readily accessible place for at least the first two years. The required records would include the following:

- All records relating to investors who purchase or attempt to purchase securities through the funding portal;[1110]

1108 The Rule is being renumbered to account for the elimination of the proposed anti-money laundering provision in proposed Rule 403(b), which is described in more detail in Section II.D.4.b. We are also adding the word "registered" to "national securities association" to be consistent with the rest of the rule text and with Exchange Act Section 3(h)(1)(B).

1109 *See* Public Startup Letter 3.

1110 This would include information relating to educational materials provided to investors, account openings and transactions, including notices of investment commitments and reconfirmations.

- All records relating to issuers that offer and sell, or attempt to offer and sell, securities through the funding portal and to persons having control with respect to those issuers;
- Records of all communications that occur on or through its platform;
- All records related to persons that use communication services provided by a funding portal to promote an issuer's securities or to communicate with potential investors;
- All records demonstrating a funding portal's compliance with requirements of Subparts C (intermediary obligations) and D (additional funding portal requirements);[1111]
- All notices provided by the funding portals to issuers and investors generally through the funding portal's platform or otherwise;[1112]
- All written agreements (or copies thereof) entered into by a funding portal, relating to its business as such;
- All daily, monthly and quarterly summaries of transactions effected through the funding portal;[1113] and

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1111 This requirement alone would not, however, require the creation of any records or proscribe the format or manner of any records. However, without records, it would be difficult for a funding portal to demonstrate compliance with Subparts C and D to examiners.

1112 These would include, but not be limited to: (1) notices addressing hours of funding portal operations (if any); (2) funding portal malfunctions; (3) changes to funding portal procedures; (4) maintenance of hardware and software; (5) instructions pertaining to access to the funding portal; and (6) denials of, or limitations on, access to the funding portal.

1113 These would include: (1) issuers for which the target offering amount has been reached and funds distributed; and (2) transaction volume, expressed in number of transactions, number of securities involved in a transaction and total amounts raised by and distributed to issuers, as well as total dollar amounts raised across all issuers, expressed in U.S. dollars.

- A log reflecting the progress of each issuer who offers and sells securities through the funding portal toward meeting the target offering amount.

As proposed, Rule 404(b) would require that a funding portal make and preserve its organizational documents during its operation as a funding portal and also those of any successor funding portal. These would include, but not be limited to: (1) partnership agreements; (2) articles of incorporation or charter; (3) minute books; and (4) stock certificate books (or other similar type documents).

We also proposed in Rule 404(c) that the records required to be maintained and preserved pursuant to Rule 404(a) be produced, reproduced, and maintained in the original, non-alterable format in which they were created or as permitted under Section 17a-4(f) of the Exchange Act. We proposed in Rule 404(d) to allow third parties to prepare or maintain the required records on behalf of the funding portal, provided that there is a written undertaking in place between the funding portal and the third party stating that the required records are the property of the funding portal and will be surrendered promptly, on request by the funding portal, to the Commission or the national securities association of which the funding portal is a member.[1114] The funding portal

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[1114] The written undertaking would be required to include the following provision:

> With respect to any books and records maintained or preserved on behalf of [name of funding portal], the undersigned hereby acknowledges that the books and records are the property of [name of funding portal], and hereby undertakes to permit examination of such books and records at any time, or from time to time, during business hours by representatives of the Securities and Exchange Commission, and the national securities association of which the funding portal is a member, and to promptly furnish to the Commission and national securities association of which the funding portal is a member, a true, correct, complete and current hard copy of any, all, or any part of, such books and records.

This provision is consistent with the recordkeeping provisions applicable to brokers under Exchange Act Rules 17a-4(f) (17 CFR 17a-4(f)) and 17a-4(j) (17 CFR 240.17a-4(j)), but has been scaled to be more appropriate for funding portals.

also would have been required to file, with the registered national securities association of which it is a member, this written undertaking, signed by a duly authorized representative of the third party. As proposed, an agreement between a funding portal and a third party would not relieve the funding portal of its responsibility to prepare and maintain records, as required under Rule 404 of Regulation Crowdfunding.

As proposed, Rule 404(e) would require all records of a funding portal to be subject at any time, or from time to time, to such reasonable periodic, special or other examination by our representatives and representatives of the registered national securities association of which the funding portal is a member.

Finally, we proposed in Rule 404(f) that funding portals would be required to comply with the reporting, recordkeeping and record retention requirements of Chapter X of Title 31 of the Code of Federal Regulations. Where Chapter X of Title 31 and proposed rules 404(a) and 404(b) would require the same records or reports to be preserved for different periods of time, we proposed requiring the records or reports to be preserved for the longer period of time.

b. Comments on Proposed Rule

Commenters generally did not object to the proposed recordkeeping requirements. Some commenters suggested that the cost for a funding portal to maintain the proposed books and records would not be significant.[1115] A few commenters suggested that funding portals should maintain required records for a longer period of time. One of these commenters recommended a retention period of 10 years,[1116] while the other suggested that issuer data should be kept

[1115] *See, e.g.*, CFIRA Letter 1, Joinvestor Letter.

[1116] *See* Joinvestor Letter.

permanently accessible by the funding portal.[1117] Another commenter suggested that the Commission should require intermediaries, rather than the issuers, to maintain records (or arrange for third-party recordkeeping) of the offering materials used by the issuers, thereby reducing the burden on issuers by no longer requiring them to transcribe offering materials into something that can be filed with EDGAR.[1118]

c. Final Rules

We are adopting Rule 404 as proposed, with a modification to subparagraph (e) to require that books and records subject to review under the subsection be produced promptly to representatives of the Commission and the national securities association of which the funding portal is a member,[1119] and a minor modification to subparagraph (f) related to anti-money laundering related records.[1120] We also made a modification to state that, in addition to being furnished to representatives of the Commission, books and records would have to be furnished to the Commission itself. We are also adding the word "registered" to "national securities association" to be consistent with the rest of the rule text and with Exchange Act Section 3(h)(1)(B).[1121]

We believe that it is important for funding portals to be subject to the recordkeeping requirements in order to create a meaningful record of crowdfunding transactions and

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1117 Mollick, *et al* Letter. *See also* Public Startup Letter 5 (suggesting that the Commission should improve "forensic record-keeping obligations of a funding portal" by requiring portals to "maintain the URLs and website content in perpetuity for all issuers who use the portal to raise capital from the public.").

1118 CFIRA Letter 1.

1119 We are making this change to remain consistent with the prompt production standard that is required for third party recordkeeping undertakings pursuant to Rule 404(d).

1120 In the Proposing Release and as noted in this section, we have provided examples of the types of information that would be required to be maintained under each of the specified records. The same guidance applies with respect to application of the final rules.

1121 Conforming changes were made to both Rules 404(d) and (e).

communications. For example, we are requiring records of all notices provided by the funding portals to issuers and investors generally through the funding portal's platform or otherwise. We believe that, in addition to the list of examples provided in the rule, this encompasses any notices relating to the funding portal's business as such, including communications in electronic form sent from an associated person of a funding portal to issuers or investors (including potential investors). Every funding portal is required under Rule 404 to furnish promptly to the Commission and its representatives, and the registered national securities association of which the funding portal is a member, legible, true, complete and current copies of such records of the funding portal that are requested by the representatives of the Commission and the national securities association.[1122]

The requirements will enable regulators to more effectively gather information about the activities in which a funding portal has been engaged, as well as about the other parties involved in crowdfunding (*e.g.*, issuers, promoters, and associated persons), to discern whether the funding portals and the other parties are in compliance with the requirements of Regulation Crowdfunding and any other applicable federal securities laws. We believe the requirements will assist regulators' compliance examinations because, without these records, the Commission and any registered national securities association of which the funding portal is a member may have difficulty examining a funding portal for compliance with the requirements of Regulation

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[1122] The Commission generally interprets the term "promptly" or "prompt" to mean making reasonable efforts to produce records that are requested by the staff during an examination without delay. The Commission believes that in many cases a funding portal could, and therefore will be required to, furnish records immediately or within a few hours of a request. The Commission expects that only in unusual circumstances would a funding portal be permitted to delay furnishing records for more than 24 hours. *Accord* Security-Based Swap Data Repository Registration, Duties, and Core Principles, Exchange Act Release No. 74246 (Feb. 11, 2015), 80 FR 14438, 14500 n. 846 (Mar. 19, 2015) (similarly interpreting the term "promptly" in the context of Exchange Act Rule 13n–7(b)(3)); Registration of Municipal Advisors, Exchange Act Release No. 70462 (Sept. 20, 2013), 78 FR 67468, 67578-67579 n. 1347 (Nov. 12, 2013) (similarly interpreting the term "prompt" in the context of Exchange Act Rule 15Ba1-8(d)).

Crowdfunding and the federal securities laws.[1123] Therefore, we believe the record retention requirements should be mandatory rather than voluntary as suggested by one commenter. Although we are not requiring that funding portals utilize the record retention services of broker-dealers, as suggested by one commenter, we note that a funding portal may find it cost-effective or otherwise appropriate to use the recordkeeping services of a third party, and the final rules provide the necessary flexibility to allow funding portals to utilize these options.

While some commenters suggest a longer record retention period, we believe the requirement that funding portals preserve their records for five years, with the records retained in a readily accessible place for at least the first two years, provides sufficient investor protection, while not imposing overly burdensome recordkeeping costs.[1124] We are not adopting, as commenters recommended, a requirement that funding portals be required to keep issuer data permanently accessible or maintain URLs and website content in perpetuity for all issuers, as we believe the permanent storage of such information could be unduly burdensome and is unnecessary.

Because permissible funding portal activity is far more limited than that of broker-dealers and a relatively high proportion of funding portals will be new market entrants that have not been subject to regulation before (rather than broker-dealers switching their business models to become funding portals) and, therefore, may not have formal recordkeeping practices in place, the recordkeeping requirements for funding portals are relatively streamlined compared to those for

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1123 *See*, *supra*, note 798.

1124 We note that the record retention period requirement continues for a funding portal after it withdraws its registration. Schedule D of Form Funding Portal requests information about the location(s) of where a funding portal will keep its books and records after withdrawal.

broker-dealers. Funding portals are intended to be subject to less regulation than broker-dealers, and recordkeeping requirements adopted in the final rules are consistent with this intent.

Finally, as described above, we are not adopting the proposed requirement that a funding portal comply with the BSA.[1125] Nevertheless, we are revising the final recordkeeping rule to require a funding portal to maintain books and records related to BSA requirements, should funding portals become subject to the requirements of the BSA.[1126]

Commission staff expects to review the books and records practices of intermediaries during the study of the federal crowdfunding exemption that it plans to undertake no later than three years following the effective date of Regulation Crowdfunding.[1127]

E. Miscellaneous Provisions

1. Insignificant Deviations from Regulation Crowdfunding

a. Proposed Rules

We proposed Rule 502 of Regulation Crowdfunding to provide issuers a safe harbor for insignificant deviations from a term, condition or requirement of Regulation Crowdfunding. As proposed in Rule 502(a), to qualify for the safe harbor, the issuer relying on the exemption would have to show that: (1) the failure to comply with a term, condition or requirement was insignificant with respect to the offering as a whole; and (2) the issuer made a good faith and reasonable attempt to comply with all applicable terms, conditions and requirements of Regulation

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1125 *See* Section II.D.4.b.

1126 15 U.S.C. 5311 *et seq.* To the extent that funding portals become subject to the requirements of the BSA and are required to comply with BSA recordkeeping requirements, we believe that this recordkeeping requirement will be valuable to our regulatory oversight function of funding portals' compliance with such BSA requirements. *See generally Recordkeeping by Brokers and Dealers*, Release No. 34-18321 (Dec. 10, 1981) [46 FR 61454 (Dec. 17, 1981)] (noting the effectiveness of on-site examinations of broker-dealers by the Commission and SROs in enforcing compliance with reporting and recordkeeping requirements when adopting Exchange Act Rule 17a-8). Rule 17a-8 (17 CFR 240.17a-8) requires broker-dealers to comply with the reporting, recordkeeping and record retention rules adopted under the BSA.

1127 *See* Section II.

Crowdfunding; and (3) the issuer did not know of the failure to comply, where the failure to comply with a term, condition or requirement was the result of the failure of the intermediary to comply with the requirements of Section 4A(a) and the related rules, or such failure by the intermediary occurred solely in offerings other than the issuer's offering. As proposed in Rule 502(b), notwithstanding this safe harbor, any failure to comply with Regulation Crowdfunding would nonetheless be actionable by the Commission.

b. Comments on the Proposed Rules

Commenters were generally in favor of the proposed safe harbor.[1128] However, some commenters representing state securities regulators suggested that the safe harbor is unnecessary, would be detrimental to state enforcement efforts and would be a burden on regulators when issuers assert the safe harbor, whether or not they were operating in good faith.[1129] These commenters also recommended that the proposed safe harbor, if adopted, should not be a defense to an enforcement action by the states.[1130]

c. Final Rules

We are adopting the Rule 502(a) safe harbor as proposed.[1131] The first two prongs of the safe harbor provision in Rule 502(a) are modeled after a similar provision in Rule 508 of Regulation D,[1132] and we believe a similar safe harbor is appropriate for offerings made in reliance on Section 4(a)(6). We believe that provisions for insignificant deviations serve an important function by allowing for certain errors that can occur in the offering process without

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1128 *See, e.g.*, Arctic Island Letter 7; CFIRA Letter 1; Heritage Letter; Joinvestor Letter; Parsont Letter; Schwartz Letter.

1129 *See* Commonwealth of Massachusetts Letter; NASAA Letter.

1130 *Id.*

1131 *See* Rule 502 of Regulation Crowdfunding.

1132 17 CFR 230.508.

causing the issuer to lose the exemption and incur certain consequences, including potential private rights of action for rescission for violations of Section 5 of the Securities Act,[1133] and loss of preemption for state securities law registration requirements. The offering exemption in Section 4(a)(6) was designed to help alleviate the funding gap and the accompanying regulatory challenges faced by startups and small businesses, many of which may not be familiar with the federal securities laws. We continue to believe that issuers should not lose the Section 4(a)(6) exemption because of insignificant deviations from a term, condition or requirement of Regulation Crowdfunding, so long as the issuer, in good faith, attempted to comply with the rules. We note that whether a deviation from the requirements would be significant to the offering as a whole will depend on the facts and circumstances of the offering and the deviation. While such determinations will be based on the particular facts and circumstances, we believe that a deviation from certain fundamental requirements in the rules, such as a failure to adhere to the aggregate offering limit under Rule 100(a)(1), presumptively would not be an insignificant deviation that would allow reliance on this safe harbor.

We are adopting the third prong of the safe harbor in Rule 502(a) because, under the statute, an issuer could lose the exemption and potentially violate Section 5 because of the failure of the intermediary to comply with the requirements of Section 4A(a). We believe that an issuer should not lose the offering exemption due to a failure by the intermediary, which likely will be out of the issuer's control, if the issuer did not know of such failure or such failure related to offerings other than the issuer's offering. Absent this safe harbor, we believe that issuers may be hesitant to participate in offerings in reliance on Section 4(a)(6) due to uncertainty about their

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[1133] *See* Securities Act Section 12(a)

ability to rely on, and to control their ongoing eligibility for, the exemption, which could undermine the facilitation of capital raising for startups and small businesses.

We believe that the potential harm to investors that might result from the applicability of this safe harbor would be minimal because the deviations must be insignificant to the offering as a whole for the safe harbor to apply. We also believe the safe harbor appropriately protects an issuer who made a diligent attempt to comply with the rules from losing the exemption as a result of insignificant deviations from Regulation Crowdfunding.

We also are adopting Rule 502(b) largely as proposed to set forth clearly that the safe harbor for insignificant deviations in Rule 502(a) does not preclude the Commission from bringing an enforcement action seeking appropriate relief for an issuer's failure to comply with all applicable terms, conditions, and requirements of Regulation Crowdfunding. Despite the suggestion of two commenters,[1134] we are not extending Rule 502(b) to enforcement actions by the states. While we recognize the concerns of certain state securities regulators that the safe harbor could be detrimental to state enforcement efforts, we believe that a state's review as to whether there is an insignificant deviation from our rules would create undue uncertainty for issuers seeking to rely on the Section 4(a)(6) exemption.[1135] We note that, irrespective of the scope of the safe harbor, states retain antifraud authority in all cases.

2. Restrictions on Resales

a. Proposed Rules

Section 4A(e) provides that securities issued in reliance on Section 4(a)(6) may not be transferred by the purchaser for one year after the date of purchase, except when transferred: (1) to

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1134 *See* Commonwealth of Massachusetts Letter; NASAA Letter.

1135 Securities Act Section 18(b)(4)(C), as amended by the JOBS Act, preempts state securities laws' registration and qualification requirements for offerings made pursuant to Section 4(a)(6). 15 U.S.C. 77r(b)(4)(C).

the issuer of the securities; (2) to an accredited investor; (3) as part of an offering registered with the Commission; or (4) to a family member of the purchaser or the equivalent, or in connection with certain events, including death or divorce of the purchaser, or other similar circumstances, in the discretion of the Commission. Section 4A(e) further provides that the Commission may establish additional limitations on securities issued in reliance on Section 4(a)(6).

Proposed Rule 501 largely tracked the provisions of Section 4A(e). We also proposed definitions of "accredited investor" and a "member of the family of the purchaser or the equivalent." Under the proposed rules, the term "accredited investor" would have the same definition in Rule 501 of Regulation D.[1136]

The statute does not define "member of the family of the purchaser or the equivalent." We proposed to define the phrase to include a "child, stepchild, grandchild, parent, stepparent, grandparent, spouse or spousal equivalent, sibling, mother-in-law, father-in-law, son-in-law, daughter-in-law, brother-in-law, or sister-in-law of the purchaser, and shall include adoptive relationships." This definition tracks the definition of "immediate family" in Exchange Act Rule 16a-1(e),[1137] but with the addition of "spousal equivalent."

b. Comments on the Proposed Rules

Two commenters supported the proposed restrictions on resales,[1138] while several other commenters opposed any resale restrictions.[1139] Two commenters expressed support for the

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1136 17 CFR 230.501(a).

1137 17 CFR 240.16a-1(e).

1138 *See* Arctic Island Letter 7; Joinvestor Letter.

1139 *See, e.g.*, Amram Letter 2 (stating resale restrictions prevent trading liquidity and impede price discovery); Crowdstockz Letter; Hamman Letter; Kickstarter Coaching Letter; Public Startup Letter 2 (recommending a six-month holding period so long as the issuer is current in its filing requirements, except that purchasers who self-certify that they are low-income investors would not be subject to a holding period); Public Startup Letter 3 (also opposing accredited investors having an advantage over other buyers).

proposal that to sell securities purchased in a transaction made in reliance on Section 4(a)(6) to an accredited investor during the restricted period, the seller of such securities would need to have a reasonable belief that the purchaser is an accredited investor.[1140]

One commenter noted that the investors who are eligible to purchase securities from the initial purchasers in the first year would be able to circumvent the investment limits of the proposed rules by purchasing securities from the initial purchasers in an amount greater than they would be able to purchase through intermediaries.[1141] Another commenter noted that the restrictions on resale appear only to cover the sale by the initial purchaser, thus creating the possibility that securities of a particular issuer could become widely traded within the first year if the initial purchaser sells the securities to an eligible purchaser who then resells them to the public within the first year.[1142]

c. Final Rules

We are adopting the restrictions on resales in Rule 501 as proposed, with certain revisions as described below.[1143] We are concerned that, as noted by several commenters, the restrictions on resales would cover only the sale by the initial purchaser, which creates the possibility that securities of a particular issuer could become widely traded within the first year if the initial purchaser sells the securities to an eligible purchaser who subsequently resells them to the public

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1140 *See* Joinvestor Letter; Public Startup Letter 3.

1141 *See* Moskowitz Letter.

1142 CrowdCheck Letter 3 (recommending several alternatives: (1) designate the securities as "restricted" within the meaning of Rule 144; (2) mirror some or all of the issuer's resale restrictions; (3) impose a one-year obligation on the issuer not to register the transfer of securities by any person, except in the four permitted types of transfers; or (4) remove the words "by the purchaser" from the first sentence of proposed Rule 501(a)).

1143 *See* Rule 501 of Regulation Crowdfunding.

within the first year. Further, the proposed rule could allow, as one commenter noted,[1144] investors to circumvent the investment limits in the first year by purchasing securities from the initial purchasers. In response to these concerns, we have modified Rule 501 from the proposal so that the one-year resale restriction will apply to any purchaser during the one-year period beginning when the securities were first issued, not just the initial purchaser. In addition, we have modified the definition to track more closely the language in Securities Act Rule 501(a) to clarify that the person reselling the securities must have a reasonable belief that the purchaser qualifies as an accredited investor.

As adopted, the rule provides that securities issued in a transaction pursuant to Section 4(a)(6) may not be transferred by any purchaser of such securities during that one-year period unless such securities are transferred: (1) to the issuer of the securities; (2) to an accredited investor; (3) as part of an offering registered with the Commission; or (4) to a member of the family of the purchaser or the equivalent, to a trust controlled by the purchaser, to a trust created for the benefit of a member of the family of the purchaser or the equivalent, or in connection with the death or divorce of the purchaser or other similar circumstance. We recognize that several commenters expressed concerns about the exception for resales to accredited investors and the potential unfair advantage this could provide to such investors. While we appreciate these concerns, we note that this treatment will provide some measure of liquidity for holders of these securities within the first year of the offering without undermining the investor protections otherwise provided by the statute and our rules.

[1144] *See* Moskowitz Letter.

3. Information Available to States

Under Section 4A(d), the Commission shall make available, or shall cause to be made available by the relevant intermediary, the information required under Section 4A(b) and such other information as the Commission, by rule, determines appropriate to the securities commission (or any agency or office performing like functions) of each state and territory of the United States and the District of Columbia. We proposed to require issuers to file on EDGAR the information required by Section 4A(b) and the related rules. Information filed on EDGAR is publicly available and would, therefore, be available to each state, territory and the District of Columbia. As we stated in the Proposing Release, we believe this approach will satisfy the statutory requirement to make the information available to each state and territory of the United States, and the District of Columbia. Commenters who addressed this issue agreed with our proposed approach,[1145] and we are adopting this provision as proposed.

4. Exemption from Section 12(g)

a. Proposed Rule

Section 303 of the JOBS Act amended Exchange Act Section 12(g) to provide that "the Commission shall, by rule, exempt, conditionally or unconditionally, securities acquired pursuant to an offering made under [S]ection 4[(a)](6) of the Securities Act of 1933 from the provisions of this subsection." As amended by the JOBS Act, Section 12(g) requires, among other things, that an issuer with total assets exceeding $10,000,000 and a class of securities held of record by either 2,000 persons, or 500 persons who are not accredited investors, register such class of securities

[1145] *See, e.g.*, CFIRA Letter 9; Public Startup Letter 3.

with the Commission.[1146] Crowdfunding contemplates the issuance of securities to a large number of holders, which could increase the likelihood that Section 4(a)(6) issuers would exceed the thresholds for triggering reporting obligations under Section 12(g). As discussed in the Proposing Release, Section 303 could be read to mean that securities acquired in a crowdfunding transaction would be excluded from the record holder count permanently, regardless of whether the securities continue to be held by a person who purchased in the crowdfunding transaction. An alternative reading could provide that securities acquired in a crowdfunding transaction would be excluded from the record holder count only while held by the original purchaser in the Section 4(a)(6) transaction, as a subsequent purchaser of the securities would not be considered to have "acquired [the securities] pursuant to an offering made under [S]ection 4[(a)](6)."

Consistent with the statute, the Commission's proposed Rule 12g-6 would provide that securities issued pursuant to an offering made under Section 4(a)(6) would be permanently exempted from the record holder count under Section 12(g). An issuer seeking to exclude a person from the record holder count would have the responsibility for demonstrating that the securities held by the person were initially issued in an offering made under Section 4(a)(6).

b. Comments on the Proposed Rules

Commenters generally supported the permanent exemption from the record holder count under Section 12(g).[1147] One commenter recommended that the exemption from the record holder count under Section 12(g) apply to different securities issued in a subsequent restructuring,

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1146 *See* Section 501 of the JOBS Act. In the case of an issuer that is a bank or a bank holding company, Exchange Act Section 12(g)(1)(B) (15 U.S.C. 78*l*(g)(1)(B)) requires, among other things, that the issuer, if it has total assets exceeding $10,000,000 and a class of securities held of record by 2,000 persons, register such class of securities with the Commission. *See* Section 601 of the JOBS Act.

1147 *See, e.g.*, ABA Letter; Arctic Island Letter 7; Craw Letter; Heritage Letter; Joinvestor Letter; PeoplePowerFund Letter; Public Startup Letter 3; Wefunder Letter.

recapitalization or similar transaction that is exempt from, or otherwise not subject to, the registration requirements of Section 5, if the parties to the transaction are affiliates of the original issuer.[1148] A few commenters recommended conditioning the exemption from the record holder count under Section 12(g) on the issuer's asset value,[1149] while a few others opposed such concept.[1150] Another commenter recommended that issuers that fail to comply with Regulation Crowdfunding's ongoing reporting requirements be disqualified from relying on the exemption from the record holder count under Section 12(g),[1151] while two commenters opposed such concept.[1152]

c. Final Rules

In response to comments received, we are adopting Rule 12g-6 with certain modifications.[1153] The rule provides that securities issued pursuant to an offering made under Section 4(a)(6) are exempted from the record holder count under Section 12(g), provided that the issuer is current in its ongoing annual reports required pursuant to Rule 202 of Regulation Crowdfunding, has total assets as of the end of its last fiscal year not in excess of $25 million, and has engaged the services of a transfer agent registered with the Commission pursuant to Section 17A of the Exchange Act.[1154]

1148 *See* Arctic Island Letter 7. *See also* ABA Letter (recommending that the Commission, at a minimum, exempt from the Section 12(g) record holder count securities issued in a statutory merger to change the domicile of the issuer, in reliance on Securities Act Rule 145(a)(2)).

1149 *See, e.g.*, ABA Letter ($25 million); PeoplePowerFund Letter.

1150 *See, e.g.*, Arctic Island Letter 7; Public Startup Letter 3.

1151 *See* Joinvestor Letter.

1152 *See* Arctic Island Letter 7; Public Startup Letter 3.

1153 17 CFR 240.12g-6.

1154 *Id.*

An issuer that exceeds the $25 million total asset threshold, in addition to exceeding the thresholds in Section 12(g), will be granted a two-year transition period before it will be required to register its class of securities pursuant to Section 12(g), provided it timely files all its ongoing reports pursuant to Rule 202 of Regulation Crowdfunding during such period.[1155] Section 12(g) registration will be required only if, on the last day of the fiscal year the company has total assets in excess of the $25 million total asset threshold, the class of equity securities is held by more than 2,000 persons or 500 persons who are not accredited investors.[1156] In such circumstances, an issuer that exceeds the thresholds in Section 12(g) and has total assets of $25 million or more will be required to begin reporting under the Exchange Act the fiscal year immediately following the end of the two-year transition period.[1157] An issuer entering Exchange Act reporting will be considered an "emerging growth company" to the extent the issuer otherwise qualifies for such status.[1158]

An issuer seeking to exclude a person from the record holder count has the responsibility for demonstrating that the securities held by the person were initially issued in an offering made under Section 4(a)(6). As noted in the proposal, we believe that allowing issuers to sell securities pursuant to Section 4(a)(6) without becoming Exchange Act reporting issuers is consistent with the intent of Title III.[1159] In this regard, we note that Title III provides for an alternative reporting

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1155 *Id.*

1156 15 U.S.C. 78*l*(g).

1157 17 CFR 240.12g-6.

1158 Under Section 2(a)(19) of the Securities Act, an "emerging growth company" is defined as, among other things, an issuer that had total annual gross revenues of less than $1 billion during its most recently completed fiscal year. 15 U.S.C. 77b(a)(19). *See also* Section 3(a)(80) of the Exchange Act (which repeats the same definition). 15 U.S.C. 78c(a)(80).

1159 *See* 158 CONG. REC. S1829 (daily ed. Mar. 20, 2012) (statement of Sen. Jeff Merkley) ("It also provides a very important provision so the small investors do not count against the shareholder number that drives

system under which issuers using the crowdfunding exemption are required to file annual reports with the Commission.[1160] We believe that conditionally exempting securities issued in reliance on Section 4(a)(6) from the record holder count under Section 12(g), and thereby from the more extensive reporting obligations under the Exchange Act, is appropriate in light of the existence of the alternative ongoing reporting requirements that are tailored to the types of issuers and offerings we anticipate under Regulation Crowdfunding.

In determining to provide a conditional exemption from the provisions of Section 12(g), we have considered a number of factors. First, we believe that conditioning the exemption on the issuer being current in its ongoing reporting requirements is consistent with the intent behind the original enactment of Section 12(g) because this condition requires that relevant, current information about issuers will be made routinely available to investors and the marketplace.[1161] Second, we believe that conditioning the 12(g) exemption on crowdfunding issuers using a registered transfer agent will provide an important investor protection in this context. As discussed in Section II.C.3 above, regarding the need for an issuer to establish means to keep accurate records of its securities holders, we received a number of comments about the benefits of using a registered transfer agent. As noted above, we are not mandating the use of a transfer agent for all crowdfunding offerings, for both flexibility and cost reasons. However, we believe that requiring the use of a transfer agent is appropriate for those issuers that are seeking to have their

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companies to have to become a fully public company. That is critical and interrelates with other parts of the [crowdfunding] bill before us.”).

1160 *See* Section II.B.2 for a discussion of the requirement to file annual reports.

1161 Section 12(g) was enacted by Congress as a way to ensure that investors in over-the-counter securities about which there was little or no information, but which had a significant shareholder base, were provided with ongoing information about their investment. *See, generally, Report of the Special Study of Securities Markets of the Securities and Exchange Commission.* House Document No. 95, House Committee on Interstate and Foreign Commerce, 88th Cong., 1st Sess. (1963), at 60-62.

crowdfunding securities exempted from the record holder count under Section 12(g). We expect that issuers at a stage at which they are seeking to rely on the Section 12(g) exemption are likely to be larger and thus better able to incur the costs of a transfer agent. In the absence of a conditional exemption from the provisions of Section 12(g), the use of a transfer agent registered under the Exchange Act would be required of issuers when they register under the Exchange Act.[1162] We note that a registered transfer agent is a regulated entity with experience in maintaining accurate shareholder records, and its use will help to ensure that security holder records and secondary trades will be handled accurately. Third, we believe that the condition of total assets not exceeding $25 million will result in phasing out the Section 12(g) exemption once companies grow and expand their shareholder base and is consistent with the intent behind Title III of the JOBS Act, which was enacted to facilitate smaller company capital formation.

Rule 12g-6 does not extend the exclusion from the Section 12(g) record holder count to different securities issued in exchange for Section 4(a)(6)-issued securities in a subsequent restructuring, recapitalization or similar transaction. While some commenters requested such an extension in instances where the parties to the transaction are affiliates of the original issuer, or in certain restructuring transactions, we do not believe that such an expansion in the context of shares initially issued using Regulation Crowdfunding would be appropriate because certain restructuring and recapitalization transactions could change the pool of holders of the securities

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[1162] Section 3(a)(25) of the Exchange Act provides that a "transfer agent" is any person who engages on behalf of an issuer of securities or on behalf of itself as an issuer of securities in: (A) countersigning such securities upon issuance; (B) monitoring the issuance of such securities with a view to preventing unauthorized issuance (i.e., a registrar); (C) registering the transfer of such securities; (D) exchanging or converting such securities; or (E) transferring record ownership of securities by bookkeeping entry without the physical issuance of securities certificates. 15 U.S.C. 78c(a)(25). Section 17A(c)(1) of the Exchange Act generally requires any person performing any of these functions with respect to any security registered pursuant to Section 12 of the Exchange Act to register with the Commission or other appropriate regulatory agency. 15 U.S.C. 78q-1(c)(1).

beyond those who initially acquired the securities in a crowdfunding transaction, denying those holders the protections of Section 12(g) registration.

5. Scope of Statutory Liability

Securities Act Section 4A(c) provides that an issuer will be liable to a purchaser of its securities in a transaction exempted by Section 4(a)(6) if the issuer, in the offer or sale of the securities, makes an untrue statement of a material fact or omits to state a material fact required to be stated or necessary in order to make the statements, in light of the circumstances under which they were made, not misleading, provided that the purchaser did not know of the untruth or omission, and the issuer does not sustain the burden of proof that such issuer did not know, and in the exercise of reasonable care could not have known, of the untruth or omission. Section 4A(c)(3) defines, for purposes of the liability provisions of Section 4A, an issuer as including "any person who offers or sells the security in such offering."

In describing the statutory liability provision in the Proposing Release, the Commission noted that it appears likely that intermediaries would be considered issuers for purposes of the provision. Several commenters agreed that Section 4A(c) liability should apply to intermediaries noting that it "may serve as a meaningful backstop against fraud"[1163] and would create a "true financial incentive" for intermediaries to conduct checks on issuers and their key personnel.[1164]

However, a large number of other commenters disagreed that Section 4A(c) liability should apply to intermediaries.[1165] Some of these commenters stated their views that applying

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1163 *See, e.g.*, Farnkoff Letter.

1164 *See, e.g.*, BackTrack Letter. *See also* Patel Letter.

1165 *See, e.g.*, ABA Letter; AngelList Letter; BetterInvesting Letter; CFIRA Letter 10; City First Letter; EarlyShares Letter; EMKF Letter; FSI Letter; Graves Letter; Guzik Letter 1; IAC Recommendation; Inkshares Letter; Milken Institute Letter; PPA Letter; RocketHub Letter; SBA Office of Advocacy Letter; SBEC Letter; SeedInvest Letter 3; Seyfarth Letter; StartupValley Letter; Wefunder Letter; Winters Letter.

statutory liability to intermediaries would have a chilling effect on intermediaries' willingness to facilitate crowdfunding offerings.[1166] Others cited the cost of being subject to this liability as overly burdensome on funding portals, to the extent that they may not be able to conduct business.[1167] Several commenters also explained that the nature of funding portals, as intended by Congress, is distinct from that of registered broker-dealers.[1168] According to these commenters, a funding portal's role is not to offer and sell securities, but rather to provide a platform through which issuers may offer and sell securities. As such, these commenters asserted that it would not be appropriate to hold them liable for statements made by issuers.[1169] In addition, one commenter suggested that applying statutory liability to funding portals, while precluding their ability to limit the offerings that they facilitate, is an "untenable" framework.[1170] Some commenters stated that the statutory construct could unnecessarily lead to lawsuits against funding portals,[1171] with one of these commenters asserting that such suits would arise "for any deal that loses money" because the burden of proof is on the funding portal to prove it could not have known of material

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1166 *See, e.g.*, Guzik Letter 1; Inkshares Letter; RocketHub Letter; StartupValley Letter.

1167 *See, e.g.*, City First Letter; Guzik Letter 1; SeedInvest Letter 3; Wefunder Letter; Winters Letter.

1168 *See, e.g.*, Inkshares Letter (likening funding portals to "impartial engineers of transactions" similar to online service providers under the Digital Millennium Copyright Act, that exist "for the transmission of information, and with it securities, between third parties"); RocketHub Letter; SeedInvest Letter 3; Seyfarth Letter.

1169 *Id.*

1170 AngelList Letter. *See also, e.g.*, Graves Letter (stating that "to achieve the appropriate balance of creating a usable crowdfunding model for small businesses while providing adequate protections for investors, the Commission should remove the liability placed on funding portals in the proposed rules or permit them to curate offerings. . . . Otherwise it is highly improbable that any rational business would establish a web portal in a heads-you-win, tails-I-lose environment"); Milken Institute Letter (noting also that funding portals should be permitted to make subjective judgments in deciding which offerings to list, including based on an assessment of the merits or shortcomings of an offering); Wefunder Letter. *See also* Section II.D.3.a (discussing Rule 402(b)(1)).

1171 *See, e.g.*, Inkshares Letter; SeedInvest Letter3.

misstatements."[1172] One commenter stated that risk disclosures should require an explanation to investors that lawsuits by investors are only potentially viable if based on claims sounding in fraud or negligence and that "lawsuits cannot be filed just because the retail investor loses their risk capital."[1173]

One commenter suggested that the Commission retract its statement in the Proposing Release that "it appears likely that intermediaries, including funding portals, would be considered issuers for purposes of this liability provision."[1174] Other commenters suggested that the Commission should take action, such as: (i) exempting funding portals from liability, provided conditions are met such as compliance with Regulation Crowdfunding[1175] or disclosure of the specific steps the funding portal has taken in its due diligence;[1176] (ii) providing a safe harbor for activities funding portals can undertake in posting issuer materials on their platforms,[1177] and (iii) providing a list of reasonable steps funding portals can take in reviewing an offering in order to rely on the reasonable care defense.[1178]

We have considered the comments both in support of and against funding portals being considered issuers for purposes of Section 4A(c) liability. Specifically, we acknowledge commenters' concerns that statutory liability may adversely affect funding portals, and

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1172 *See* SeedInvest Letter 3.

1173 *See* CarbonTech Letter.

1174 *See* SeedInvest Letter 3.

1175 CFIRA Letter 10; SeedInvest Letter 3 (stating also that directors and officers of funding portals should be excluded from the definition of "issuer" for purposes of the statutory provision); StartupValley Letter.

1176 EarlyShares Letter.

1177 CFIRA Letter 10; StartupValley Letter.

1178 CFIRA Letter 10; Milken Institute Letter (stating that funding portals "should not be required to 'look behind' every material statement in an offering, but rather should be held to a standard of satisfying the statute's and proposed rule's steps for ensuring that an offering does not invoke concerns of fraud or investor protection"); StartupValley Letter.

suggestions that, under the statutory scheme, funding portals and broker-dealers engage in different activities that do not warrant a funding portal being subject to statutory liability. One difference commenters highlighted was the inability of a funding portal to limit the offerings on its platform under the proposed rules, and the untenable position of imposing statutory liability while precluding funding portals' ability to limit the offerings on their platforms. In response to this comment, as described above, we have modified the language of the Rule 402 safe harbor from the proposal to permit funding portals to exercise discretion to limit the offerings and issuers that they allow on their platforms.[1179] We believe this will avoid the "untenable" framework that commenters described. We are specifically declining to exempt funding portals (or any intermediaries) from the statutory liability provision of Section 4A(c) or to interpret this provision as categorically excluding such intermediaries. We do not believe that we should preclude the ability of investors to bring private rights of action against funding portals (or any intermediaries). Such a categorical exemption or exclusion could pose undue risks to investors by providing insufficient incentives for intermediaries to take steps to prevent their platforms from becoming vehicles for fraud.

Accordingly, we believe that the determination of "issuer" liability for an intermediary under Section 4A(c) will turn on the facts and circumstances of the particular matter in question. While we acknowledge the concerns of commenters about the potential application of Section 4A(c) liability, we note that Congress provided a defense to any such liability if an intermediary did not know, and in the exercise of reasonable care could not have known, of the untruth or omission. We continue to believe, as we identified in the Proposing Release, that there are appropriate steps that intermediaries might take in exercising reasonable care in light of this

[1179] *See* Rule 402(b)(1); Section II.D.3.a.

liability provision. These steps may include establishing policies and procedures[1180] that are reasonably designed to achieve compliance with the requirements of Regulation Crowdfunding, and conducting a review of the issuer's offering documents, before posting them to the platform, to evaluate whether they contain materially false or misleading information.

6. Disqualification Provisions

Section 302(d) of the JOBS Act requires the Commission to establish disqualification provisions under which an issuer would not be eligible to offer securities pursuant to Section 4(a)(6) and an intermediary would not be eligible to effect or participate in transactions pursuant to Section 4(a)(6). Section 302(d)(2) specifies that the disqualification provisions must be "substantially similar" to the "bad actor" disqualification provisions contained in Rule 262 of Regulation A[1181] and they also must cover certain actions by state regulators enumerated in Section 302(d)(2).

The disqualification provisions included in Section 302(d) of the JOBS Act are modeled on the disqualification provisions included in Section 926 of the Dodd-Frank Act, which also required the Commission to adopt rules "substantially similar" to Rule 262 of Regulation A that disqualify securities offerings involving certain "felons and other 'bad actors'" from reliance on Rule 506 of Regulation D. On July 10, 2013, we adopted rules to implement Section 926 of the Dodd-Frank Act to disqualify certain securities offerings from reliance on Rule 506 of Regulation

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1180 With respect to intermediaries that are funding portals, see Rule 403(a) of Regulation Crowdfunding and the discussion in Section II.D.4.

1181 17 CFR 230.262.

D.[1182] On March 25, 2015, we adopted amendments to Rule 262 of Regulation A[1183] that made those provisions substantially similar to those adopted under Rule 506 of Regulation D.

a. Issuers and Certain Other Associated Persons

(1) Proposed Rules

As described in more detail below, the proposed disqualification rules as they relate to issuers and certain other associated persons would have been substantially similar to the disqualification rules in Rules 262 and 506. Under those rules, disqualification arises only with respect to events occurring after effectiveness of the rules and disqualified persons may seek a waiver from the Commission from application of the disqualification provisions.

(2) Comments on Proposed Rules

Commenters were generally supportive of the proposed disqualification rules.[1184] A few commenters recommended that pre-existing events should be subject to the disqualification rules,[1185] although another supported the proposed approach of imposing disqualification only for events after effectiveness.[1186] One commenter recommended that the Commission expand the list

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1182 See Disqualification of Felons and Other "Bad Actors" from Rule 506 Offerings, Release No. 33-9414 (July 10, 2013) [78 FR 44729 (July 24, 2013)] ("Disqualification Adopting Release").

1183 *See* Rule 506(c) Adopting Release, *supra*, note 5.

1184 *See, e.g.*, ABA Letter (expressing general support and recommending the Commission provide guidance on the term "voting securities" and regarding the waiver process); Commonwealth of Massachusetts Letter; Consumer Federation Letter (expressing an understanding of why the proposed disqualification rules are consistent with those under Regulation D, but noting their belief that those rules were weak when adopted); FundHub Letter 1 (stating that the proposed disqualification rules "are, to a certain degree, overkill" and too costly, but that disqualifying bad actors is good for the future of equity crowdfunding); Joinvestor (supporting the proposed look-back periods and waiver rules). *But see* Public Startup Letter 3 (stating the proposed rules are unconstitutional without explaining its reasoning); Public Startup Letter 5 (recommending the Commission establish an "offender registry" that requires issuers to maintain a "public profile" containing information about potential issuers in a standardized format, similar to FINRA's BrokerCheck).

1185 *See, e.g.*, Guzik Letter 1; NASAA Letter.

1186 *See* Joinvestor Letter.

of covered persons to include transfer agents and lawyers who are subject to certain disqualifications.[1187]

(3) Final Rules

We are adopting bad actor disqualification provisions for Regulation Crowdfunding[1188] substantially as proposed with the exception of several modifications to further align the final rules with similar provisions in Rules 262 and 506. We believe that the final rules are appropriate in light of the JOBS Act Section 302(d) mandate. We further believe that creating a uniform set of bad actor standards for all exemptions that include bad actor disqualification is likely to simplify due diligence, particularly for issuers that may engage in different types of exempt offerings.

Under the final disqualification rules, covered persons include the issuer and any predecessor of the issuer or affiliated issuer; directors, officers, general partners or managing members of the issuer; beneficial owners of 20% or more of the issuer's outstanding voting equity securities (which we believe should be calculated based on the present right to vote for the election of directors, irrespective of the existence of control or significant influence); any promoter connected with the issuer in any capacity at the time of such sale; compensated solicitors of investors; and general partners, directors, officers or managing members of any such solicitor.[1189] We have not expanded the list of covered persons, as suggested by a commenter, because we believe that the limited additional investor protection that such an expansion may

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1187 *See* Brown J. Letter (also recommending the Commission adopt similar bad actor provisions under Rule 504).

1188 *See* Rule 503 of Regulation Crowdfunding.

1189 *See* Rule 503(a) of Regulation Crowdfunding.

provide would not justify the costs that would result from inconsistent bad actor disqualification rules.

The disqualifying events include:

- felony and misdemeanor convictions within the last five years in the case of issuers, their predecessors and affiliated issuers, and 10 years in the case of other covered persons in connection with the purchase or sale of a security, involving the making of a false filing with the Commission; or arising out of the conduct of the business of an underwriter, broker, dealer, municipal securities dealer, investment adviser, funding portal or paid solicitor of purchasers of securities;[1190]
- injunctions and court orders within the last five years against engaging in or continuing conduct or practices in connection with the purchase or sale of securities; involving the making of any false filing with the Commission; or arising out of the conduct of the business of an underwriter, broker, dealer, municipal securities dealer, investment adviser, funding portal or paid solicitor of purchasers of securities;[1191]
- certain final orders and bars of certain state and other federal regulators;[1192]
- Commission cease-and-desist orders relating to violations of scienter-based anti-fraud provisions of the federal securities laws or Section 5 of the Securities Act;[1193]
- filing, or being named as an underwriter in, a registration statement or Regulation A offering statement that is the subject of a proceeding to determine whether a stop order or

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1190 *See* Rule 503(a)(1) of Regulation Crowdfunding.

1191 *See* Rule 503(a)(2) of Regulation Crowdfunding.

1192 *See* Rule 503(a)(3) of Regulation Crowdfunding.

1193 *See* Rule 503(a)(5) of Regulation Crowdfunding.

suspension should be issued, or as to which a stop order or suspension was issued within the last five years;[1194]

- United States Postal Service false representation orders within the last five years;[1195] and
- for covered persons other than the issuer:
    - being subject to a Commission order:
        - revoking or suspending their registration as a broker, dealer, municipal securities dealer, investment adviser or funding portal;
        - placing limitations on their activities as such;
        - barring them from association with any entity; or
        - barring them from participating in an offering of penny stock;[1196] or
    - being suspended or expelled from membership in, or suspended or barred from association with a member of, a registered national securities exchange or national securities association for conduct inconsistent with just and equitable principles of trade.[1197]

Consistent with Rules 262 and 506 and the proposal, we also are adopting provisions allowing for a waiver from and a reasonable care exception to the disqualification provisions.[1198] Under the final rules, an issuer will not lose the benefit of the Section 4(a)(6) exemption if it is able to show that it did not know, and in the exercise of reasonable care could not have known, of

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1194 *See* Rule 503(a)(7) of Regulation Crowdfunding.

1195 *See* Rule 503(a)(8) of Regulation Crowdfunding.

1196 *See* Rule 503(a)(4) of Regulation Crowdfunding.

1197 *See* Rule 503(a)(6) of Regulation Crowdfunding.

1198 *See* Rule 503(b) of Regulation Crowdfunding.

the existence of a disqualification.[1199] Further, persons that are disqualified from relying on the exemption may request a waiver of disqualification from the Commission.[1200]

The final rules also specify that triggering events that pre-date effectiveness of the final rules will not cause disqualification, but instead must be disclosed on a basis consistent with Rules 262 and 506(e).[1201] Specifically, issuers will be required to disclose in their offering materials matters that would have triggered disqualification had they occurred after the effective date of proposed Regulation Crowdfunding.[1202] In a change from the proposal, Rule 201(u) does not include the word "timely" as is included in Rule 506(e) of Regulation D, because unlike the disclosure associated with Rule 506(e), the disclosure required by Rule 201(u) must be included in an issuer's offering statement and thus is required to be timely to the offering.

We believe this disclosure will put investors on notice of events that would, but for the timing of such events, have disqualified the issuer from relying on Section 4(a)(6). We also believe that this disclosure is particularly important because, as a result of the implementation of Section 302(d), investors may have the impression that all bad actors are disqualified from participating in offerings under Section 4(a)(6). If disclosure of a pre-existing, otherwise disqualifying event is required and not provided to an investor, we would not view this as an insignificant deviation from Regulation Crowdfunding under Rule 502.

Consistent with the proposal and with Rule 506, the final disqualification rules provide that events relating to certain affiliated issuers are not disqualifying if the events pre-date the affiliate relationship. Specifically, Rule 503(c) provides that events relating to any affiliated

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1199 *See* Rule 503(b)(4) of Regulation Crowdfunding.

1200 *See* Rule 503(b)(2) of Regulation Crowdfunding.

1201 *See* Rules 201(u) and 503(b)(1) of Regulation Crowdfunding.

1202 *See* Rule 201(u) of Regulation Crowdfunding.

issuer that occurred before the affiliation arose will be not considered disqualifying if the affiliated entity is not (1) in control of the issuer or (2) under common control with the issuer by a third party that was in control of the affiliated entity at the time of such events.[1203]

We also have modified the final rules to expressly include funding portals in the list of entities that could be subject to felony and misdemeanor convictions, injunctions and court orders that would constitute disqualifying events.[1204] As proposed, funding portals would have been included because they meet the definition of broker; however, for clarity, the final rule expressly includes them.

b. Intermediaries and Certain Other Associated Persons

(1) Proposed Rules

Section 302(d)(1)(B) requires the Commission to establish disqualification provisions under which an intermediary would not be eligible to effect or participate in transactions conducted pursuant to Securities Act Section 4(a)(6). Section 302(d)(2) requires that the disqualification provisions be substantially similar to the provisions of Securities Act Rule 262, which applies to issuers. Exchange Act Section 3(a)(39)[1205] currently defines the circumstances in which a broker would be subject to a "statutory disqualification" with respect to membership or participation in a self-regulatory organization such as FINRA or any other registered national

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1203 *See* Rule 503(c) of Regulation Crowdfunding.

1204 *See* Rules 503(a)(1)(iii) and 503(a)(2)(iii) of Regulation Crowdfunding. Because funding portals are brokers within the meaning of Exchange Act Section (3)(a)(4) (albeit exempt from registration as such), we believe that they would be covered by the term "broker" in the final rule. Nevertheless, for clarity, we are adding funding portals to the final rule text to avoid any confusion in this regard.

1205 15 U.S.C. 78c(39).

securities association. We believe that the definition of "statutory disqualification" under Section 3(a)(39) is substantially similar to, while somewhat broader than, the provisions of Rule 262.[1206]

As proposed, Rule 503(d) would have prohibited any person subject to a statutory disqualification as defined in Exchange Act Section 3(a)(39) from acting as, or being an associated person of, an intermediary unless permitted to do so by Commission rule or order. The term "subject to a statutory disqualification" has an established meaning under Exchange Act Section 3(a)(39) and defines circumstances that subject a person to a statutory disqualification with respect to membership or participation in, or association with a member of, a self-regulatory organization.[1207] Because funding portals, like broker-dealers, are required to be members of FINRA or any other applicable registered national securities association, we anticipate that funding portals will take appropriate steps to check the background of any person seeking to become associated with them, including whether such person is subject to a statutory disqualification.

In addition, we proposed to clarify that associated persons of intermediaries engaging in transactions in reliance on Section 4(a)(6) must comply with Exchange Act Rule 17f-2,[1208] relating to the fingerprinting of securities industry personnel. Under the proposal, Exchange Act

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1206 See the Proposing Release at note 812 for a discussion of differences between Exchange Act Section 3(a)(39) and Rule 262. Despite the differences, we believe that Section 3(a)(39) and Rule 262 are substantially similar, in particular with regard to the persons and events they cover, their scope and their purpose.

1207 Events that could result in a statutory disqualification for an associated person under Section 3(a)(39) include, but are not limited to: certain misdemeanor and all felony criminal convictions; temporary and permanent injunctions issued by a court of competent jurisdiction involving a broad range of unlawful investment activities; expulsions (and current suspensions) from membership or participation in an SRO; bars (and current suspensions) ordered by the Commission or an SRO; denials or revocations of registration by the CFTC; and findings by the Commission, CFTC or an SRO that a person: (1) "willfully" violated the federal securities or commodities laws, or the Municipal Securities Rulemaking Board (MSRB) rules; (2) "willfully" aided, abetted, counseled, commanded, induced or procured such violations; or (3) failed to supervise another who commits violations of such laws or rules. 15 U.S.C. 78c(a)(39).

1208 17 CFR 240.17f-2.

Rule 17f-2 would have applied to all brokers, including registered funding portals. The proposed instruction to Rule 503(d) would have clarified that Rule 17f-2 generally requires the fingerprinting of every person who is a partner, director, officer or employee of a broker, subject to certain exceptions.

(2) Final Rules

We are adopting Rule 503(d) as proposed. We received two comments on the proposed rule. One commenter was in favor,[1209] while another commenter was opposed.[1210] The Section 3(a)(39) standard is an established one among financial intermediaries and their regulators. For this reason, we believe the Section 3(a)(39) standard is more appropriate for intermediaries than Rule 262 or the issuer disqualification rules under Regulation Crowdfunding. We are concerned that if we imposed a new or different statutory disqualification standard only for those intermediaries that engage in transactions in reliance on Section 4(a)(6), we may create confusion and unnecessary burdens on market participants. We note that such a divergence in standards would cause brokers that act as intermediaries in reliance on Section 4(a)(6) (and their associated persons) to become subject to two distinct standards for disqualification. Instead, we believe that intermediaries should be subject to the same statutory disqualification standard regardless of whether or not they are engaging in transactions involving the offer or sale of securities in reliance on Section 4(a)(6), and note that applying consistent standards for all brokers and funding portals will also assist FINRA or any other registered national securities association in its oversight of its members. Further, Exchange Act Rule 19h-1 prescribes the form and content of, and establishes the mechanism by which the Commission reviews, proposals submitted by SROs (such as

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1209 *See* NASAA Letter.

1210 *See* Public Startup Letter 3.

FINRA) for its members, to allow a member or associated person subject to a statutory disqualification to become or remain a member or be associated with a member ("notice of admission or continuance notwithstanding a statutory disqualification," as described in Rule 19h-1(a)). Among other things, Rule 19h-1 provides for Commission review of notices filed by SROs proposing to admit any person to, or continue any person in, membership or association with a member notwithstanding a statutory disqualification as defined in Section 3(a)(39). Because intermediaries are required to be members of a registered national securities association (which is an SRO), actions taken by the SRO with respect to a proposed admission or continuance with respect to an intermediary or its associated persons will be subject to Rule 19h-1. Thus, the "pursuant to Commission rule" provision in Rule 503(d) will be satisfied if the admission or continuance request was subject to the requirements and process of Exchange Act Rule 19h-1. We also are adopting, as proposed, the instruction to Rule 503(d) clarifying that the Rule 17f-2 fingerprinting requirements are applicable to all associated persons of intermediaries engaging in transactions in reliance on Section 4(a)(6).

7. Secondary Market Trading

In addition to the actions the Commission is taking today to permit the offer and sale of securities in reliance on Section 4(a)(6), the Commission also recently adopted rules that exempt from the registration requirements of the Securities Act certain offerings of up to $50 million of securities annually,[1211] and rules to eliminate the prohibition against general solicitation in certain offerings pursuant to Regulation D under the Securities Act.[1212] The Commission is mindful of

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[1211] *See* Regulation A Adopting Release, *supra*, note 506.

[1212] *See* Rule 506(c) Adopting Release, *supra*, note 5.

the need for market participants to have updated information in connection with the secondary market trading of securities issued pursuant to these rules.[1213]

The anti-fraud provisions of the federal securities laws, and rules adopted thereunder, apply to the secondary market trading of securities, including securities offered and sold in reliance on Section 4(a)(6). For example, Exchange Act Rule 15c2-11 governs broker-dealers' publication of quotations for certain over-the-counter securities in a quotation medium other than a national securities exchange.[1214] The Commission adopted Rule 15c2-11 to prevent fraudulent and manipulative trading schemes that had arisen in connection with the distribution and trading of certain unregistered securities.[1215] The rule prohibits broker-dealers from publishing quotations (or submitting quotations for publication) in a "quotation medium"[1216] for covered over-the-counter securities without first reviewing basic information about the issuer, subject to certain exceptions.[1217] A broker-dealer also must have a reasonable basis for believing that the issuer information is accurate in all material respects and that it was obtained from a reliable source.[1218]

[1213] As discussed in Section II.E.2, Rule 501 imposes a one-year restriction on the transfer of securities issued in a transaction exempt from registration pursuant to Section 4(a)(6) of the Securities Act, other than to the issuer, an accredited investors, or to a family member of the purchaser or the equivalent in connection with certain specified events.

[1214] 17 CFR 240.15c2-11.

[1215] *See generally* Initiation or Resumption of Quotations by a Broker or Dealer Who Lacks Certain Information, Exchange Act Release No. 9310 (Sept. 13, 1971), 36 FR 18641 (Sept. 18, 1971). *See also* Publication or Submission of Quotations Without Specified Information, Exchange Act Release No. 39670 (Feb. 17, 1998), 63 FR 9661, 9662 (Feb. 25, 1998).

[1216] 17 CFR 240.15c2-11(e)(1) (defining quotation medium as "any 'interdealer quotation system' or any publication or electronic communications network or other device which is used by brokers or dealers to make known to others their interest in transactions in any security, including offers to buy or sell at a stated price or otherwise, or invitations of offers to buy or sell").

[1217] 17 CFR 240.15c2-11(a). See Publication or Submission of Quotations Without Specified Information, Exchange Act Release No. 34-39670 (Feb. 17, 1998), 63 FR 9661 (Feb. 25, 1998).

[1218] *Id*.

To be clear, the rules adopted today do not affect the obligations of a broker-dealer under Exchange Rule 15c2-11 to have a reasonable basis under the circumstances for believing that the information required by Rule 15c2-11 is accurate in all material respects, and that the sources of the information are reliable, prior to publishing any quotation, absent an exception,[1219] for a covered security in any quotation medium.[1220] The staff is directed to begin promptly an evaluation of the operation of Rule 15c2-11, both historically and in light of recent market developments, including Regulation Crowdfunding and earlier proposals for amendments to Rule 15c2-11,[1221] to assess how the rule is meeting regulatory objectives and to recommend any appropriate changes. In addition, and not withstanding any changes which may be made to Rule 15c2-11 in the interim, the staff is also directed to review the development of secondary market trading in these securities during the study it plans to undertake within three years following the effective date of Regulation Crowdfunding, and to recommend to the Commission such additional actions with respect to Rule 15c2-11, as may be warranted.[1222]

1219 *See* 17 CFR 240.15c2-11(f). For example, the rule includes an exception for unsolicited orders. 17 CFR 240.15c2-11(f)(2). We remind broker-dealers that such unsolicited orders must be made by a customer (other than a person acting as or for a dealer) and that broker-dealers should be prepared to demonstrate that a customer initiated the order. 17 CFR 240.15c2-11(b)(1).

1220 Rule 15c2-11(c) further requires that broker-dealers keep the documents that they reviewed to establish this reasonable basis for believing that the required information is accurate in all material respects for a period of not less than three years. 17 CFR 240.15c2-11(c). The lack of documents used at the time the broker-dealer established the reasonable basis for its belief or presentation of incomplete or non-responsive documents, including later-dated filings, would not be sufficient to demonstrate that the broker-dealer had satisfied its obligations in this regard. See Initiation or Resumption of Quotations Without Specified Information, Exchange Act Release No 27247 (Sept. 14, 1989), 54 FR 39194, 39196 (Sept. 25, 1989) ("Subject to certain exceptions, the Rule prohibits a broker or dealer from submitting a quotation for a security in a quotation medium unless it has in its records specified information concerning the security and the issuer. . .").

1221 *See* Exchange Act Release No. 41110 (Feb. 25, 1999), 64 FR 11124 (Mar. 8, 1999).

1222 *See* Section II.

III. ECONOMIC ANALYSIS

Title III sets forth a comprehensive regulatory structure for startups and small businesses to raise capital through securities-based crowdfunding transactions using the Internet. In particular, Title III provides an exemption from registration for certain offerings of securities by adding Securities Act Section 4(a)(6). In addition, Title III:

- adds Securities Act Section 4A, which requires, among other things, that issuers and intermediaries that facilitate transactions between issuers and investors provide certain information to investors, take certain actions and provide notices and other information to the Commission;
- adds Exchange Act Section 3(h), which requires the Commission to adopt rules to exempt, either conditionally or unconditionally, funding portals from having to register as broker-dealers or dealers pursuant to Exchange Act Section 15(a)(1);
- mandates that the Commission adopt disqualification provisions under which an issuer would not be able to avail itself of the exemption for crowdfunding if the issuer or other related parties, including an intermediary, were subject to a disqualifying event; and
- adds Exchange Act Section 12(g)(6), which requires the Commission to adopt rules to exempt from Section 12(g), either conditionally or unconditionally, securities acquired pursuant to an offering made in reliance on Section 4(a)(6).

As discussed in detail above, we are adopting Regulation Crowdfunding to implement the requirements of Title III. The final rules implement the new exemption for the offer and sale of securities pursuant to the requirements of Section 4(a)(6) and provide a framework for the regulation of issuers and intermediaries, which include broker-dealers and funding portals

engaging in such transactions. The final rules also permanently exempt securities offered and sold in reliance on Section 4(a)(6) from the record holder count under Exchange Act Section 12(g).

We are mindful of the costs imposed by, and the benefits to be obtained from, our rules. Securities Act Section 2(a) and Exchange Act Section 3(f) require us, when engaging in rulemaking that requires us to consider or determine whether an action is necessary or appropriate in the public interest, to consider, in addition to the protection of investors, whether the action will promote efficiency, competition and capital formation. Exchange Act Section 23(a)(2) requires us, when adopting rules under the Exchange Act, to consider the impact that any new rule would have on competition and to not adopt any rule that would impose a burden on competition that is not necessary or appropriate in furtherance of the purposes of the Exchange Act. The discussion below addresses the economic effects of the final rules, including the likely costs and benefits of Regulation Crowdfunding, as well as the likely effect of the final rules on efficiency, competition and capital formation. Given the specific language of the statute and our understanding of Congress's objectives, we believe that it is appropriate for the final rules generally to follow the statutory provisions. We nonetheless also rely on our discretionary authority to adopt certain additional provisions and make certain other adjustments to the final rules. While the costs and benefits of the final rules in large part stem from the statutory mandate of Title III, certain costs and benefits are affected by the discretion we exercise in connection with implementing this mandate. For purposes of this economic analysis, we address the costs and benefits resulting from the mandatory statutory provisions and our exercise of discretion together because the two types of benefits and costs are not separable.

A. Baseline

The baseline for our economic analysis of Regulation Crowdfunding, including the baseline for our consideration of the effects of the final rules on efficiency, competition and capital formation, is the situation in existence today, in which startups and small businesses seeking to raise capital through securities offerings must register the offer and sale of securities under the Securities Act unless they can rely on an existing exemption from registration under the federal securities laws. Moreover, under existing requirements, intermediaries intending to facilitate such transactions generally are required to register with the Commission as broker-dealers under Exchange Act Section 15(a).

1. Current Methods of Raising up to $1 Million of Capital

The potential economic impact of the final rules, including their effects on efficiency, competition and capital formation, will depend on how the crowdfunding method of raising capital compares to existing methods that startups and small businesses currently use for raising capital. Startups and small businesses can potentially access a variety of external financing sources in the capital markets through registered or unregistered offerings of debt, equity and hybrid securities and bank loans.

Issuers seeking to raise capital must register the offer and sale of securities under the Securities Act or qualify for an exemption from registration. Registered offerings, however, are generally too costly to be viable alternatives for startups and small businesses. Issuers conducting registered offerings incur Commission registration fees, legal and accounting fees and expenses, transfer agent and registrar fees, costs associated with periodic reporting requirements and other regulatory requirements and various other fees. Two surveys concluded that the average initial compliance cost associated with conducting an initial public offering is $2.5 million, followed by

an ongoing compliance cost for issuers, once public, of $1.5 million per year.[1223] Hence, for an issuer seeking to raise less than $1 million, a registered offering may not be economically feasible.[1224] Moreover, issuers conducting registered offerings also usually pay underwriter fees, which are, on average, approximately 7% of the proceeds for initial public offerings, approximately 5% for follow-on equity offerings and approximately 1−1.5% for issuers raising capital through public bond issuances.[1225]

An alternative to raising capital through registered offerings is to offer and sell securities by relying on an existing exemption from registration under the federal securities laws. For example, startups and small businesses could rely on current exemptions from registration under the Securities Act, such as Section 3(a)(11),[1226] Section 4(a)(2),[1227] Regulation D,[1228] and

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1223 *See* IPO Task Force, *Rebuilding the IPO On-Ramp*, at 9 (Oct. 20, 2011) for the two surveys, *available at* http://www.sec.gov/info/smallbus/acsec/rebuilding_the_ipo_on-ramp.pdf ("IPO Task Force"). These estimates should be interpreted with the caveat that most firms in the IPO Task Force surveys likely raised more than $1 million. The IPO Task Force surveys do not provide a breakdown of costs by offering size. However, compliance related costs of an initial public offering and subsequent compliance related costs of being a reporting company likely have a fixed cost component that would disproportionately affect small offerings.

Title I of the JOBS Act provided certain accommodations to issuers that qualify as emerging growth companies (EGCs). According to a recent working paper, the underwriting, legal and accounting fees of EGC and non-EGC initial public offerings were similar (based on a time period from April 5, 2012 to April 30, 2014). For a median EGC initial public offering, gross spread comprised 7% of proceeds and accounting and legal fees comprised 2.4% of proceeds. *See* Susan Chaplinsky, Kathleen W. Hanley, and S. Katie Moon, *The JOBS Act and the Costs of Going Public*, Working Paper (2014), *available at* http://ssrn.com/abstract_id=2492241.

1224 *Id.*

1225 *See, e.g.*, Hsuan-Chi Chen and Jay R. Ritter, *The Seven Percent Solution*, 55 J. FIN. 1105−1131 (2000); Mark Abrahamson, Tim Jenkinson, and Howard Jones, *Why Don't U.S. Issuers Demand European Fees for IPOs*? 66 J. FIN. 2055–2082 (2011); Shane A. Corwin, *The Determinants of Underpricing for Seasoned Equity Offers*, 58 J. FIN. 2249−2279 (2003); Lily Hua Fang, *Investment Bank Reputation and the Price and Quality of Underwriting Services*, 60 J. FIN. 2729−2761 (2005); Rongbing Huang and Donghang Zhang, *Managing Underwriters and the Marketing of Seasoned Equity Offerings*, 46 J. FIN. QUANT. ANALYSIS 141–170 (2011); Stephen J. Brown, Bruce D. Grundy, Craig M. Lewis and Patrick Verwijmeren, *Convertibles and Hedge Funds as Distributors of Equity Exposure*, 25 REV. FIN. STUD. 3077−3112 (2012).

1226 Securities Act Section 3(a)(11), generally known as the "intrastate offering exemption," provides an exemption from registration for issuers doing business within a particular state or territory. To qualify for this exemption, the offering must be "part of an issue offered and sold only to persons resident within a

Regulation A.[1229] While we do not have complete data on offerings relying on an exemption under Section 3(a)(11) or Section 4(a)(2), certain data available from Regulation D and Regulation A filings allow us to gauge how frequently issuers seeking to raise up to $1 million use these exemptions.

Based on Regulation D filings by issuers that are not pooled investment vehicles from 2009 to 2014,[1230] a substantial number of issuers chose to raise capital by relying on Rule 506, even though their offering size would qualify for an exemption under Rule 504 or Rule 505.[1231] The 2013 amendment to Rule 506 of Regulation D permits an issuer to engage in general solicitation and general advertising in offering and selling securities pursuant to Rule 506(c), subject to certain conditions,[1232] which can enable issuers to reach a potentially broader base of accredited investors. As shown in the table below, although issuers can raise unlimited amounts of capital relying on the Rule 506(c) exemption, most of the issuers made offers for amounts of up to $1 million.

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single State or Territory, where the issuer of such security is a person resident and doing business within, or, if a corporation, incorporated by and doing business within, such State or Territory."

1227 Securities Act Section 4(a)(2) provides that the registration provisions of the Securities Act shall not apply to "transactions by an issuer not involving a public offering."

1228 Regulation D provides exemptions and a nonexclusive safe harbor from registration for certain types of securities offerings.

1229 Regulation A provides a conditional exemption from registration for certain small issuances.

1230 *See* Scott Bauguess, Rachita Gullapalli, and Vladimir Ivanov, *Capital Raising in the U.S.: An Analysis of the Market for Unregistered Securities Offerings, 2009–2014* (October 2015) ("*Unregistered Offerings White Paper*"), *available at*: http://www.sec.gov/dera/staff-papers/white-papers/unregistered-offering10-2015.pdf.

1231 This tendency could, in part, be attributed to two features of Rule 506: preemption from state registration ("blue sky") requirements and an unlimited offering amount. *See also* U.S. Government Accountability Office, *Factors That May Affect Trends in Regulation A Offerings*, GAO-12-839 (Jul. 3, 2012), *available at* http://www.gao.gov/products/GAO-12-839 ("GAO Report").

1232 In particular, all purchasers of securities sold in any offering under the exemption must be accredited investors, and the issuer must take reasonable steps to verify that purchasers of securities sold in any offering are accredited investors (17 CFR 230.506). *See* Rule 506(c) Adopting Release, *supra*, note 5.

Regulation D exemption	Offering size			
	≤$1 Million	$1-5 million	$5-50 million	>$50 million
Rule 504	3,643	--	--	--
Rule 505	501	774	--	--
Rule 506(b)	27,106	25,746	18,670	2,733
Rule 506(c)	588	531	419	89
Total	31,838	27,051	19,089	2,822
Regulation A	5	33	--	--

Note: Data based on Form D, excluding issuers that are pooled investment vehicles, and Form 1-A filings from 2009 to 2014. We consider only new offerings and exclude offerings with amounts sold reported as $0 on Form D. Data on Rule 506(c) offerings covers the period from September 23, 2013 (the day the rule became effective) to December 31, 2014. We also use the maximum amount indicated in Form 1-A to determine offering size for Regulation A offerings.[1233]

Based on the table above, from 2009 to 2014, almost no issuers in offerings of up to $1 million relied on Regulation A. This data does not reflect the recent changes to Regulation A adopted by the Commission on March 25, 2015. Those changes allow issuers to raise up to $50 million over a 12-month period and exempt certain Regulation A offerings (Tier 2 offerings) from state registration requirements. Because these changes are so recent, more time is needed to observe how the amendments to Regulation A will affect capital raising by small issuers.[1234]

Each of these exemptions, however, includes restrictions that may limit its suitability for startups and small businesses. The table below lists the main requirements of these exemptions. For example, the exemption under Securities Act Section 3(a)(11) is limited to intrastate offerings.[1235] Issuers conducting a Regulation A offering may be required to register their

1233 We only consider Regulation A offerings that have been qualified by the Commission. For purposes of counting filings, we exclude amendments or multiple Form 1-A filings by the same issuer in a given year. For purposes of determining the offering size for Regulation A offerings, we use the maximum amount indicated on the latest pre-qualification Form 1-A or amended Form 1-A. We reclassify two offerings that are dividend reinvestment plans with unclear offering amounts as having the maximum permitted offering amount.

1234 *See Regulation A Adopting Release*.

1235 *See* note 1226.

offerings with states or meet additional regulatory requirements, such as investment limitations (if the investor is not an accredited investor), audited financial statements and ongoing reporting. In addition, issuers in all Regulation A offerings are required to file with the Commission an offering document on Form 1-A. Such compliance related costs may be a more significant constraint on issuers in offerings of up to $1 million.[1236] Issuers of securities pursuant to Securities Act Section 4(a)(2) and Rules 504, 505 and 506(b) under Regulation D generally may not engage in general solicitation and general advertising to reach investors, which also can place a significant limitation on offerings by startups and small businesses. While Rule 506 under Regulation D preempts the applicability of state registration requirements and new Rule 506(c) permits general solicitation and general advertising, an issuer seeking to rely on Rule 506(c) is limited to selling securities only to accredited investors.[1237]

The table below summarizes the main features of each exemption.

[1236] *See* Rutheford B. Campbell, Jr., *Regulation A: Small Businesses' Search for "A Moderate Capital"*, 31 DEL. J. CORP. L. 77, 106 (2006). *See also GAO Report*, note 1231.

[1237] *See Rule 506(c) Adopting Release*, note 5.

Type of Offering	Offering Limit[1238]	Solicitation	Issuer and Investor Requirements	Filing Requirement	Resale Restrictions	Blue Sky Law Preemption
Section 3(a)(11)	None	All offerees must be resident in state	All issuers and investors must be resident in state	None	No[1239]	No
Section 4(a)(2)	None	No general solicitation	Transactions by an issuer not involving any public offering[1240]	None	Restricted securities	No
Regulation A	Tier 1: $20 million with $6 million limit on secondary sales by affiliates of the issuer; Tier 2: $50 million with $15 million limit on secondary sales by affiliates of the issuer	Testing the waters permitted both before and after filing the offering statement	U.S. or Canadian issuers, excluding investment companies, blank-check companies, reporting companies, and issuers of fractional undivided interests in oil or gas rights, or similar interests in other mineral rights[1241]	File testing the waters materials and Form 1-A for Tiers 1 and 2; file annual, semi-annual, and current reports for Tier 2; file exit report for Tier 1 and to suspend or terminate reporting for Tier 2	No	Tier 1: No Tier 2: Yes

1238 Aggregate offering limit on securities sold within a twelve-month period.

1239 Although Section 3(a)(11) does not have explicit resale restrictions, the Commission has explained that "to give effect to the fundamental purpose of the exemption, it is necessary that the entire issue of securities shall be offered and sold to, and come to rest only in the hands of residents within the state." *See* SEC Rel. No. 33-4434 (Dec. 6, 1961) [26 FR 11896 (Dec. 13, 1961)]. State securities laws, however, may have specific resale restrictions. Securities Act Rule 147, a safe harbor under Section 3(a)(11), limits resales to persons residing in-state for a period of nine months after the last sale by the issuer. [17 CFR 230.147].

1240 Section 4(a)(2) of the Securities Act provides a statutory exemption for "transactions by an issuer not involving any public offering." *See SEC v. Ralston Purina Co.* 346 U.S. 119 (1953) (holding that an offering to those who are shown to be able to fend for themselves is a transaction "not involving any public offering.")

1241 The Regulation A exemption also is not available to companies that have been subject to any order of the Commission under Exchange Act Section 12(j) entered within the past five years; have not filed ongoing reports required by the regulation during the preceding two years, or are disqualified under the regulation's "bad actor" disqualification rules.

Type of Offering	Offering Limit[1238]	Solicitation	Issuer and Investor Requirements	Filing Requirement	Resale Restrictions	Blue Sky Law Preemption
Rule 504 Regulation D	$1 million	General solicitation permitted in some cases[1242]	Excludes investment companies, blank-check companies, and Exchange Act reporting companies	File Form D[1243]	Restricted in some cases[1244]	No
Rule 505 Regulation D	$5 million	No general solicitation	Unlimited accredited investors and up to 35 non-accredited investors	File Form D[1245]	Restricted securities	No
Rule 506(b) Regulation D	None	No general solicitation	Unlimited accredited investors and up to 35 non-accredited investors	File Form D[1246]	Restricted securities	Yes
Rule 506(c) Regulation D	None	General solicitation is permitted subject to certain conditions [1247]	Unlimited accredited investors; no non-accredited investors	File Form D[1248]	Restricted securities	Yes

2. Current Sources of Funding for Startups and Small Businesses that Could Be Substitutes or Complements to Crowdfunding

At present, startups and small businesses can raise capital from several sources that could be close substitutes for or complements to crowdfunding transactions that rely on Section 4(a)(6). This capital raising generally is conducted through unregistered securities offerings, involves lending by financial institutions or derives from family and friends.

1242 No general solicitation or advertising is permitted unless the offering is registered in a state requiring the use of a substantive disclosure document or sold under a state exemption for sales to accredited investors with general solicitation.

1243 Filing is not a condition of the exemption, but it is required under Rule 503.

1244 Restricted unless the offering is registered in a state requiring the use of a substantive disclosure document or sold under a state exemption for sale to accredited investors.

1245 Filing is not a condition of the exemption, but it is required under Rule 503.

1246 Filing is not a condition of the exemption, but it is required under Rule 503.

1247 General solicitation and general advertising are permitted under Rule 506(c), provided that all purchasers are accredited investors and the issuer takes reasonable steps to verify accredited investor status.

1248 Filing is not a condition of the exemption, but it is required under Rule 503.

a. Family and Friends

Family and friends are sources through which startups and small businesses can raise capital. This source of capital is usually available early in the lifecycle of a small business, before the business engages in arm's-length and more formal funding channels.[1249] Among other things, family and friends may donate funds, loan funds or acquire an equity stake in the business. A recent study of the financing choices of startups finds that most of the capital supplied by friends and family is in the form of loans.[1250] In contrast to a commercial lender that, for example, would need to assess factors such as the willingness and ability of a borrower to repay the loan and the viability of its business, family and friends may be willing to provide capital based primarily or solely on personal relationships. Family and friends, however, may be able to provide only a limited amount of capital compared to other sources. In addition, financial arrangements with family and friends may not be an optimal source of funding if any of the parties is not knowledgeable about the structuring of loan agreements, equity investments or related areas of accounting. We do not have data available on these financing sources that allow us to quantify their magnitude and compare them to other current sources of capital.

1249 *See* Paul Gompers and Josh Lerner, THE VENTURE CAPITAL CYCLE (MIT Press 2006) ("Gompers"); Alicia M. Robb and David T. Robinson, *The Capital Structure Decisions of New Firms*, 27 REV. FIN. STUD. 153-179 (2014) ("Robb").

1250 *See* Robb, note 1249.

b. Commercial Loans, Peer-to-Peer Loans and Microfinance

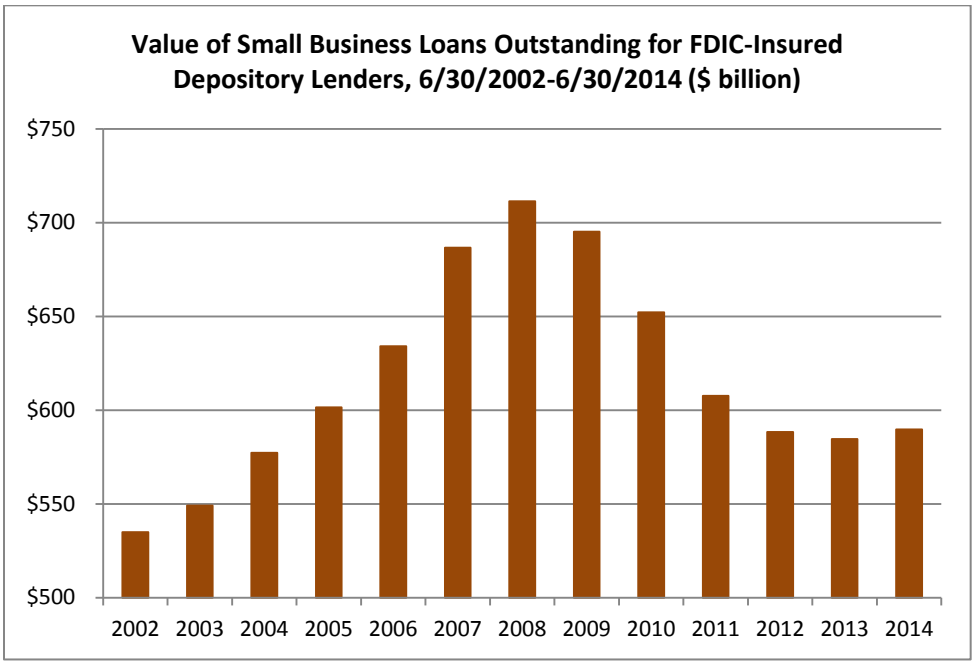
Startups and small businesses also may seek loans from financial institutions.[1251] A 2014 study of the financing choices of startups suggests that they resort to bank financing early in their lifecycle.[1252] The study finds that businesses rely heavily in the first year after being formed on external debt sources such as bank financing, mostly in the form of personal and commercial bank loans, business credit cards and credit lines. Another recent report, however, suggests that bank lending to small businesses fell by $100 billion from 2008 to 2011 and that, by 2012, less than one-third of small businesses reported having a business bank loan.[1253] Trends in small business lending by FDIC-insured depository institutions are illustrated in the figure below. As of June 2014, business loans of up to $1 million amounted to approximately $590 billion, approximately 17% lower than the 2008 level.[1254]

1251 Using data from the 1993 Survey of Small Business Finance, one study indicates that financial institutions account for approximately 27% of small firms' borrowings. *See* Allen N. Berger and Gregory F. Udell, *The Economics of Small Business Finance: The Roles of Private Equity and Debt Markets in the Financial Growth Cycle*, 22 J. BANKING & FIN. 613 (1998). *See also* 1987, 1993, 1998 and 2003 Surveys of Small Business Finances, *available at* http://www.federalreserve.gov/pubs/oss/oss3/nssbftoc.htm. The Survey of Small Business Finances was discontinued after 2003. Using data from the Kauffman Foundation Firm Surveys, one study finds that 44% of startups use loans from financial institutions. *See* Rebel A. Cole and Tatyana Sokolyk, *How Do Start-Up Firms Finance Their Assets? Evidence from the Kauffman Firm Surveys* (2012), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2028176.

1252 *See* Robb, note 1249.

1253 *See* The Kauffman Foundation, *2013 State of Entrepreneurship Address* (Feb. 5, 2013), *available at* http://www.kauffman.org/uploadedFiles/DownLoadableResources/SOE%20Report_2013pdf. The report cautions against prematurely concluding that banks are not lending enough to small businesses as the sample period of the study includes the most recent recession.

1254 We define small business loans to include commercial and industrial loans to U.S. addressees of up to $1 million and loans secured by nonfarm nonresidential properties. *See* Federal Deposit Insurance Corporation, *Statistics on Depository Institutions Report*, *available at* http://www2.fdic.gov/SDI/SOB/ ("FDIC Statistics").



Additionally, although covering the pre-recessionary period, a Federal Reserve Board staff study analyzing data from the 2003 Survey of Small Business Finance suggests that 60 percent of small businesses have outstanding credit in the form of a credit line, a loan or a capital lease.[1255] These loans were borrowed from two types of financial institutions – depositary and non-depositary institutions (*e.g.*, finance companies, factors or leasing companies).[1256] Lines of credit were the most widely used type of credit.[1257] Other types included mortgage loans, equipment loans and motor vehicle loans.[1258]

Various loan guarantee programs of the Small Business Administration ("SBA") make credit more accessible to small businesses by either lowering the interest rate of the loan or

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1255 *See* Federal Reserve Board, *Financial Services Used by Small Businesses: Evidence from the 2003 Survey of Small Business Finances* (October 2006), *available at* http://www.federalreserve.gov/pubs/bulletin/2006/smallbusiness/smallbusiness.pdf ("2003 Survey").

1256 *See* Rebel Cole, *What Do We Know About the Capital Structure of Privately Held Firms? Evidence from the Surveys of Small Business Finance*, 42 FIN. MANAGEMENT 777–813 (2013).

1257 *See* 2003 Survey, note 1255 (estimating that 34% of small businesses use lines of credit).

1258 *Id.*

enabling a market-based loan that a lender would not be willing to provide absent a guarantee.[1259] Although the SBA does not itself act as a lender, the agency guarantees a portion of loans made and administered by lending institutions. SBA loan guarantee programs include 7(a) loans[1260] and CDC/504 loans.[1261] For example, in SBA fiscal year 2014, the SBA supported approximately $28.7 billion in 7(a) and CDC/504 loans distributed to approximately 51,500 small businesses.[1262] SBA-guaranteed loans, however, currently account for a relatively small share (18 percent) of the balances of small business loans outstanding.[1263] The SBA also offers the Microloan program, which provides funds to specially designated intermediary lenders that administer the program for eligible borrowers.[1264]

1259 Numerous states also offer a variety of small business financing programs, such as Capital Access Programs, collateral support programs and loan guarantee programs. These programs are eligible for support under the State Small Business Credit Initiative, *available at* http://www.treasury.gov/resource-center/sb-programs/Pages/ssbci.aspx.

1260 15 U.S.C. 631 *et seq*. The 7(a) loans provide small businesses with financing guarantees for a variety of general business purposes through participating lending institutions.

1261 15 U.S.C. 695 *et seq*. The CDC/504 loans are made available through "certified development companies" or "CDCs," typically structured with the SBA providing 40% of the total project costs, a participating lender covering up to 50% of the total project costs and the borrower contributing 10% of the total project costs.

1262 *See* U.S. Small Business Administration, *FY 2016 Congressional Budget Justification and FY 2014 Annual Performance Report*, available at https://www.sba.gov/content/fiscal-year-2016-congressional-budget-justificationannual-performance-report ("2014 Annual Performance Report").

1263 As of the end of SBA fiscal year 2014, the SBA-guaranteed business loans outstanding (including 7(a) and 504 loans) equaled $107.5 billion. *See Small Business Administration Unpaid Loan Balances by Program, available at* https://www.sba.gov/sites/default/files/files/WDS_Table1_UPB_Report.pdf. This comprises approximately 18% of the approximately $590 billion in outstanding small business loans for commercial real estate and commercial and industrial loans discussed above. In 2014 the SBA expanded eligibility for loans under its business loan programs. *See* SBA *504 and 7(a) Loan Programs Updates* (Mar. 21, 2014) [79 FR 15641 (Apr. 21, 2014)]. In addition to loan guarantees, the SBA program portfolio also includes direct business loans, which are mainly microloans (outstanding direct business loans equaled $137.1 billion), and disaster loans.

1264 15 U.S.C. 631 *et seq*. The Microloan program provides small, short-term loans to small businesses and certain types of not-for-profit childcare centers. The maximum loan amount is $50,000, but the average microloan is about $13,000. Intermediaries are nonprofit community-based organizations with experience in lending, as well as management and technical assistance. Intermediaries set their own lending requirements and generally require some type of collateral as well as the personal guarantee of the business owner. *See Microloan Program*, U.S. Small Business Administration, *available at* http://www.sba.gov/content/microloan-program.

Many startups and small businesses may find loan requirements imposed by financial institutions difficult to meet and may not be able to rely on these institutions to secure funding. For example, financial institutions generally require a borrower to provide collateral and/or a guarantee,[1265] which startups, small businesses and their owners may not be able to provide. Collateral and/or a guarantee may similarly be required for loans guaranteed by the SBA.

Another source of debt financing for startups and small businesses is peer-to-peer lending, which began developing in 2005.[1266] Such debt transactions are facilitated by online platforms that connect borrowers and lenders and potentially offer small businesses additional flexibility on pricing, repayment schedules, collateral or guarantee requirements, and other terms. Some market participants offer a secondary market for loans originated on their own sites.[1267] At least one of the platforms sells third-party issued securities to multiple individual investors, thus improving the liquidity of these securities.[1268] Like in any traditional lending arrangement, however, borrowers are required to make regular payments to their lenders. This requirement could make it a less attractive option for small businesses with negative cash flows and short operating histories, both of which may make it more difficult for such businesses to demonstrate their ability to repay loans. According to some estimates, the global volume of "lending-based" crowdfunding, which

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As of the end of SBA fiscal year 2014, the SBA Microloans outstanding equaled $136.7 billion. *See Small Business Administration Unpaid Loan Balances by Program, available at* https://www.sba.gov/sites/default/files/files/WDS_Table1_UPB_Report.pdf.

1265 Approximately 92% of all small business debt to financial institutions is secured, and about 52% of that debt is guaranteed, primarily by the owners of the firm. *See* Berger, note 1251.

1266 *See* Ian Galloway, *Peer-to-Peer Lending and Community Development Finance*, Federal Reserve Bank of San Francisco, Working Paper (2009), *available at* http://www.frbsf.org/publications/community/wpapers/2009/wp2009-06.pdf.

1267 *Id.*

1268 *Id.* We note that under current law, this activity would require broker-dealer registration.

includes peer-to-peer lending to consumers and businesses, had risen to approximately $11.08 billion in 2014.[1269]

Technology has facilitated the growth of alternative models of small business lending. According to one study,[1270] the outstanding portfolio balance of online lenders has doubled every year, although this market represents less than $10 billion in outstanding loan capital as of the fourth quarter of 2013. Several models of online small business lending have emerged: online lenders raising capital from institutional investors and lending on their own account (for example, short-term loan products similar to a merchant cash advance); peer-to-peer platforms; and "lender-agnostic" online marketplaces that facilitate small business borrower access to various loan products (such as term loans, lines of credit, merchant cash advances and factoring products) from traditional and alternative lenders.[1271] According to the 2014 Small Business Credit survey,[1272] 18% of all small businesses surveyed applied for credit with an online lender. The survey also showed differences in the use of online lenders by type of borrower: 22% of small businesses categorized in the survey as "startups" (*i.e.*, businesses that have been in business for less than

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1269 *See* Massolution, *2015CF Crowdfunding Industry Report: Market Trends, Composition and Crowdfunding Platforms*, *available at* http://reports.crowdsourcing.org/index.php?route=product/product&product_id=54 ("Massolution 2015") at 56. The Massolution 2015 report refers to peer-to-peer lending to consumers and peer-to-business lending to small businesses as "lending-based" crowdfunding. The discussion in this economic analysis refers to peer-to-peer business lending more broadly in a sense synonymous with "lending-based" crowdfunding.

1270 *See* Karen Gordon Mills and Brayden McCarthy, *The State of Small Business Lending: Credit Access during the Recovery and How Technology May Change the Game*, Harvard Business School Working Paper 15-004 (2014), *available at* http://ssrn.com/abstract=2470523.

1271 *Id*.

1272 The survey was conducted by the Federal Reserve Banks of New York, Atlanta, Cleveland, and Philadelphia between September and November of 2014. It focused on credit access among businesses with fewer than 500 employees in Alabama, Connecticut, Florida, Georgia, Louisiana, New Jersey, New York, Ohio, Pennsylvania, and Tennessee. The survey authors note that since the sample is not a random sample, results were reweighted for industry, age, size, and geography to reduce coverage bias. *See* Federal Reserve Banks of New York, Atlanta, Cleveland and Philadelphia, *Joint Small Business Credit Survey Report* (2014), *available at* http://www.newyorkfed.org/smallbusiness/SBCS-2014-Report.pdf.

five years) applied for credit with online lenders. By comparison, 8% of small businesses categorized in the survey as "growers" (*i.e.*, businesses that were profitable and experienced an increase in revenue) applied with online lenders, and 3% of small businesses categorized in the survey as "mature firms" (*i.e.*, businesses that have been in business for more than five years, had over ten employees, and had prior debt) applied with an online lender. The latter two categories of small businesses were more likely to apply for credit with bank lenders than with online lenders.

Microfinance is another source of debt financing for startups and small businesses. Microfinance consists of small, working capital loans provided by microfinance institutions ("MFIs") that are invested in microenterprises or income-generating activities.[1273] The typical users of microfinance services and, in particular, of microcredit are family-owned enterprises or self-employed, low-income entrepreneurs, such as street vendors, farmers, service providers, artisans and small producers, who live close to the poverty line in both urban and rural areas.[1274]

The microfinance market has evolved and grown considerably in the past decades. While data on the size of the overall industry is sparse, according to one report, in fiscal year 2012, the U.S. microfinance industry was estimated to have disbursed $292.1 million across 36,936 microloans and was estimated to have $427.6 million in outstanding microloans (across 45,744 in microloans).[1275] As of 2013, this report identified 799 microenterprise programs that provide

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1273 *See* Craig Churchill and Cheryl Frankiewicz, *Making Microfinance Work: Managing for Improved Performance*, Geneva International Labor Organization (2006).

1274 *See* Joanna Ledgerwood, *Microfinance Handbook: An Institutional and Financial Perspective*, Washington DC, World Bank Publications (1999).

1275 *See* FIELD at the Aspen Institute, *U.S. Microenterprise Census Highlights*, FY 2012, *available at* http://fieldus.org/Publications/CensusHighlightsFY2012.pdf.

loans, training, technical assistance and other microenterprise services directly to micro-entrepreneurs.[1276]

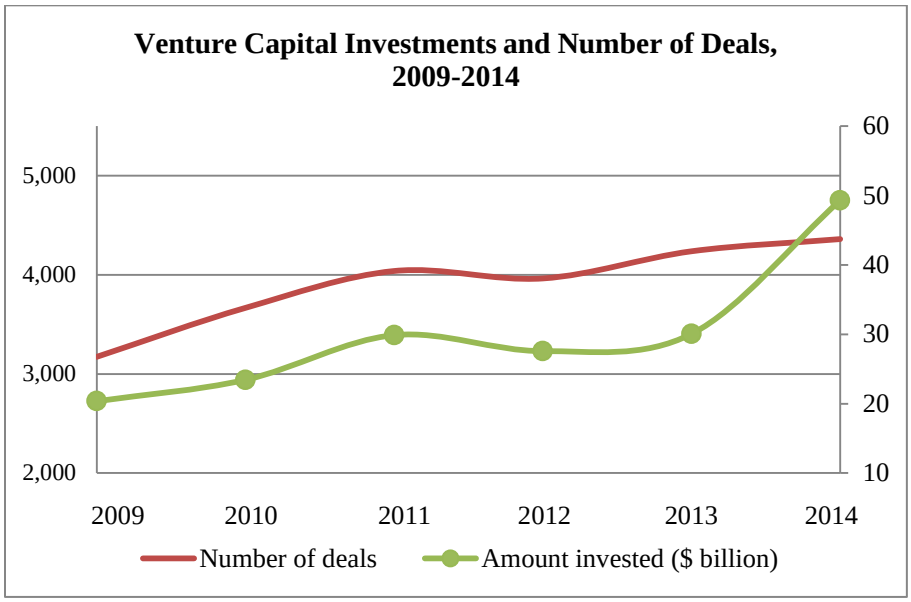
c. Venture Capitalists and Angel Investors

Startups and small businesses also may seek funding from venture capitalists ("VCs") and angel investors. Entrepreneurs seek VC and angel financing usually after they have exhausted sources of capital that generally do not require the entrepreneurs to relinquish control rights (*e.g.*, personal funds from family and friends).

According to data from the National Venture Capital Association, in calendar year 2014, VCs invested approximately $49.3 billion in 4,361 transactions involving 3,665 companies, which included seed, early-stage, expansion, and late-stage companies. Seed and early-stage deals represented 1.5% and 32.2%, respectively, of the dollar volume of deals and 4.4% and 49.7%, respectively of the overall number of VC deals.[1277]

[1276] *Id*. *See also* note 1264 (describing the SBA Microloan program).

[1277] *See* National Venture Capital Association, *2015 National Venture Capital Association Yearbook*, *available at* http://nvca.org/?ddownload=1868 ("NVCA").



Some startups, however, may struggle to attract funding from VCs because VCs tend to invest in startups with certain characteristics. A defining feature of VCs is that they tend to focus on startup companies with high-growth potential and a high likelihood of going public after a few years of financing. VCs also tend to invest in companies that have already used some other sources of financing, tend to be concentrated in certain geographic regions (*e.g.*, California and Massachusetts) and often require their investments to have an attractive business plan, meet certain growth benchmarks or fill a specific portfolio or industry niche.[1278] In addition, when investing in companies, VCs tend to acquire significant control rights (*e.g.*, board seats, rights of first refusal, *etc*.), which they gradually relinquish as the company approaches an initial public offering.[1279] In 2014, according to an industry source, information technology and medical/health/life sciences deals attracted the largest dollar volume of VC financing.[1280]

1278 *See* Gompers, note 1249.

1279 *See* Steven N. Kaplan and Per Stromberg, *Financial Contracting Meets the Real World: An Empirical Analysis of Venture Capital Contracts*, 70 REV. ECON. STUD. 281–316 (2003).

1280 *See* NVCA, note 1277.

According to a 2012 academic study, VCs appear to focus on scale or potential for scale rather than short-term profitability in their selection of targets, and firms that receive VC financing tend to be significantly larger than non-VC firms, based on employment and sales.[1281]

According to a recent report, angel investments amounted to $24.1 billion in 2014, with approximately 73,400 entrepreneurial ventures receiving angel funding and approximately 316,600 active angel investors.[1282] In 2014, angel investments were concentrated in software, healthcare, and IT services. The average angel deal size was approximately $328,500. Seed/startup stage deals accounted for 25% and early stage deals accounted for 46%.[1283] As suggested by an academic study, angel investors tend to invest in younger companies than VCs.[1284]

3. Current Crowdfunding Practices

A recent crowdfunding industry report[1285] defines the current crowdfunding activity in the United States generally as "lending-based,"[1286] "reward-based," "donation-based," "royalty-based," "equity-based,"[1287] and "hybrid." We note that the definitions of crowdfunding types

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1281 *See* Manju Puri and Rebecca Zarutskie, *On the Life Cycle Dynamics of Venture-Capital- and Non-Venture-Capital-Financed Firms*, 67 J. FIN., 2247–2293 (2012) ("Puri").

1282 *See* Jeffrey Sohl, *The Investor Angel Market in 2014: A Market Correction in Deal Size, Center for Venture Research*, May 14, 2015, *available at* https://paulcollege.unh.edu/sites/paulcollege.unh.edu/files/webform/2014%20Analysis%20Report.pdf ("Sohl").

1283 *Id*.

1284 *See* Gompers, note 1249.

1285 *See* Massolution 2015.

1286 *Id*. In this industry report, "lending-based" crowdfunding includes peer-to-peer lending to consumers and peer-to-business lending.

1287 The report does not identify which jurisdictions were represented in the survey. For example, France, Italy, Japan, and the UK have adopted specialized equity crowdfunding regimes. It should be noted that "equity-based" crowdfunding is not a one-size-fits-all model. The crowdfunding regimes in these four countries differ on a number of dimensions (*e.g.*, securities allowed to be sold by issuers, or types of issuers allowed to use the exemption), amongst themselves and when compared to Regulation Crowdfunding. Some number

used in this industry report and the characteristics of crowdfunding activity currently in existence are not directly comparable to the contours of security-based crowdfunding transactions contemplated by the rules being adopted today. Thus, considerable caution must be exercised when generating projections of future crowdfunding volume from current activity broadly attributed to the "crowdfunding" industry. In particular, the industry report defines reward-based crowdfunding as a model where funders receive a "reward," such as a perk or a pre-order of a product, and it defines donation-based crowdfunding as a model where funders make philanthropic donations to causes that they want to support, with no return on their investment expected.[1288] According to the industry report, royalty-based crowdfunding, which involves a percentage of revenue from a license or a usage-based fee for the other parties' right to the ongoing use of an asset, continues to grow.[1289]

The industry report indicates that, in 2014, crowdfunding platforms raised approximately $16.2 billion globally, which represented a 167% increase over the amount raised in 2013.[1290] These amounts include various types of crowdfunding: lending-based crowdfunding accounted for the largest share of volume (approximately $11.08 billion) followed by equity-based crowdfunding (approximately $1.11 billion), reward-based crowdfunding (approximately $1.33 billion), donation-based crowdfunding (approximately $1.94 billion), royalty-based crowdfunding

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also allow equity crowdfunding through their general securities laws. *See Eleanor Kirby and Shane Worner, Crowd-funding: An Infant Industry Growing Fast*, Staff Working Paper of the IOSCO Research Department, *available* at http://www.iosco.org/research/pdf/swp/Crowd-funding-An-Infant-Industry-Growing-Fast.pdf.

1288 *See* Massolution 2015 at 42. Many of the current domestic crowdfunding offerings relate to individual projects and may not have a defined or sustained business model commensurate with typical issuers of securities.

1289 *Id*. at 43. The Massolution 2015 report did not provide separate statistics on royalty-based and hybrid crowdfunding models prior to the 2013 report.

1290 *Id*. at 13.

(approximately $273 million), and hybrid crowdfunding (approximately $487 million).[1291] In 2014, North American crowdfunding volume was approximately $9.46 billion, which represented a 145% increase over the amount raised in 2013[1292] (including approximately $1.23 billion in reward-based crowdfunding, approximately $959 million in donation-based crowdfunding, and approximately $787.5 million in equity-based crowdfunding, with the remainder comprised of lending-based, royalty-based, and hybrid models[1293]). The industry report further indicates that global equity-based crowdfunding volume grew by 182% in 2014.[1294] According to the report, this rapid growth in equity-based crowdfunding has been driven largely by North America and Europe.[1295]

The industry report further indicates that, in 2014 the worldwide average size of a funded campaign was less than $4,000 for consumer lending-based, reward-based, and donation-based crowdfunding types.[1296] Crowdfunded business loans and equity-based campaigns, however, were substantially higher. In 2014, the global average size of a funded peer-to-business lending-based crowdfunding campaign was $103,618.[1297] In 2014, a typical equity-based campaign was larger, with the global average size of $275,461.[1298] These figures suggest that the types of ventures financed through equity-based crowdfunding could be different than those financed

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1291 *Id*. at 14.

1292 *Id*. at 53.

1293 *Id*. at 55.

1294 *Id*. at 14. By comparison, in 2014, "reward-based" crowdfunding grew by 84%, "lending-based" crowdfunding by 223%; "donation-based" crowdfunding by 45%; "royalty-based" crowdfunding by 336%; and "hybrid" crowdfunding by 290%.

1295 *Id*. at 55. "Equity-based" crowdfunding in North America ($787.5 million) and Europe ($177.5 million) grew by 301% and 145%, respectively.

1296 *Id*. at 59.

1297 *Id*. at 60.

1298 *Id*. at 60.

through other crowdfunding methods. In 2014, the average size of a funded equity-based campaign in North America was $175,000.[1299]

Since the passage of the JOBS Act, many U.S. states have made changes to their securities laws to accommodate intrastate securities-based crowdfunding transactions. Based on information from NASAA, as of September 2015, 29 states and the District of Columbia have enacted state crowdfunding provisions that rely, at the federal level, on the intrastate offering exemptions under Securities Act Section 3(a)(11) and Rule 147 or on Rule 504 of Regulation D. These state crowdfunding rules allow businesses in a state to use securities-based crowdfunding to raise capital from investors within that state.[1300] There is limited information available to us about the scope of domestic crowdfunding activity in reliance on the intrastate exemptions. Since December 2011, when the first state (Kansas) enacted its crowdfunding provisions, 118 state crowdfunding offerings have been reported to be filed with the respective state regulator and 102 were reported to be approved or cleared, as of August 1, 2015.[1301]

4. Survival Rates for Startups and Small Businesses

Startups and small businesses that lack tangible assets or business experience needed to obtain conventional financing might turn to securities-based crowdfunding in reliance on

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1299 *Id.* at 60. The report does not provide the average size of North American donation-based, reward-based, or lending-based crowdfunding campaigns. The report notes that, in 2014, the average funded North American donation-based and reward-based campaigns were 56% and 54%, respectively, of the average size of funded European donation-based and reward-based campaigns. *Id.* at 60.

1300 *See* NASAA's Intrastate Crowdfunding Resource Center at http://www.nasaa.org/industry-resources/corporation-finance/instrastate-crowdfunding-resource-center/, accessed in September 2015. *See also* NASAA's State Crowdfunding Update, *available at:* http://nasaa.cdn.s3.amazonaws.com/wp-content/uploads/2014/12/Intrastate-Crowdfunding-Overview-2015.pdf.

1301 Based on information provided by NASAA. The jurisdictions included in the estimate are Alabama, District of Columbia, Georgia, Idaho, Indiana, Kansas, Maine, Maryland, Massachusetts, Michigan, Oregon, Texas, Vermont, Washington, and Wisconsin.

Section 4(a)(6) as an attractive potential source of financing. There is broad evidence that many of these potential issuers are likely to fail after receiving funding. For example, a 2010 study reports that of a random sample of 4,022 new high-technology businesses started in 2004, only 68% survived by the end of 2008.[1302]

Similarly, other studies suggest that startups and small businesses financed by venture capitalists also tend to have high failure rates. One study finds that for 16,315 VC-backed companies that received their first institutional funding round between 1980 and 1999, approximately one-third failed after the first funding round.[1303] Additionally, another study of more than 2,000 companies that received at least $1 million in venture funding, from 2004 through 2010, finds that almost three-quarters of these companies failed.[1304] Another study, based on a sample ending in 2005, found cumulative failure rates of 34.1% for VC-financed firms and 66.3% for non-VC-financed firms, with the difference driven by lower failure rates of VC-financed firms in the initial years after receiving VC financing.[1305]

Taken all together, the failure rates documented in these studies are high for startups and small businesses, even with the involvement of sophisticated investors like VCs. Because we expect that issuers that will engage in offerings made in reliance on Section 4(a)(6) will be in an

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1302 *See* Alicia Robb, E.J. Reedy, Janice Ballou, David DesRoches, Frank Potter and Zhanyun Zhao, *An Overview of the Kauffman Firm Survey: Results from the 2004-2008 Data*, Kauffman Foundation, *available at* http://www.kauffman.org/uploadedFiles/kfs_2010_report.pdf ("Kauffman Firm Survey").

1303 *See* Yael V. Hochberg, Alexander Ljungqvist and Yang Lu, *Whom You Know Matters: Venture Capital Networks and Investment Performance*, 62 J. OF FIN. 251-301 (2007).

1304 *See* Deborah Gage, *The Venture Capital Secret: 3 Out of 4 Start-Ups Fail*, WALL ST. J., Sept. 19, 2012.

1305 *See* Puri, note 1281. According to this study, the difference in the outcomes of VC-financed and non-VC-financed firms decreases after accounting for observable differences in firm characteristics, but it does not disappear. However, as the study notes, in evaluating the remaining differences in the outcomes of VC-financed and non-VC-financed firms, it is not possible to fully differentiate the effects of superior selection on the basis of unobservable firm characteristics from the effects of VC monitoring and expertise.

earlier stage of business development than the businesses included in the above studies, we believe that issuers that engage in securities-based crowdfunding may have higher failure rates than those in the studies cited above.

5. Market Participants

The final rules will have their most significant impact on the market for the financing of startups and small businesses. The number of participants in this market and the amounts raised through alternative sources indicate that this is a large market. In 2013, there were more than 5 million small businesses, defined by the U.S. Census Bureau as having fewer than 500 paid employees.[1306] As of June 2014, FDIC-insured depositary institutions held approximately $590 billion in approximately 23.4 million small business loans.[1307] According to the SBA's fiscal year 2014 annual performance report, approximately 51,500 small businesses received funding in 2014 through SBA's main lending programs, 7(a) and 504 loans.[1308] In 2014, VCs invested $49.3 billion of capital in in 4,361 transactions involving 3,665 startups, according to an industry source.[1309] In 2014, angel investors contributed $24.1 billion, with approximately 73,400 entrepreneurial ventures receiving angel funding.[1310]

Below, we analyze the economic effect of the final rules on the following parties: (1) issuers, typically startups and small businesses, that seek to raise capital by issuing securities; (2) intermediaries through which issuers seeking to engage in transactions in reliance on

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1306 *See* U.S. Department of Commerce, United States Census Bureau, *Business Dynamics Statistics, Data: Firm Characteristics* (2013), *available at* http://www.census.gov/ces/dataproducts/bds/data_firm.html.

1307 For the purposes of this figure, small business loans are defined as loans secured by nonfarm nonresidential properties and commercial and business loans of $1,000,000 or less. *See* FDIC Statistics, note 1254.

1308 *See* 2014 Annual Performance Report, note 1262.

1309 *See* NVCA, note 1277.

1310 *See* Sohl, note 1282.

Section 4(a)(6) will offer and sell their securities; (3) investors who purchase or may consider purchasing securities in such offerings; and (4) other capital providers, broker-dealers and finders who currently participate in private offerings. The potential economic impact of the final rules will depend on how these market participants respond to the final rules. Each of these parties is discussed in further detail below.

a. Issuers

The final rules will permit certain entities to raise capital by issuing securities for the first time. The number, type and size of the potential issuers that will seek to use crowdfunding to offer and sell securities in reliance on Section 4(a)(6) is uncertain, but data on current market practices may help identify the number and characteristics of potential issuers.

It is challenging to precisely predict the number of future securities offerings that might rely on Section 4(a)(6), particularly because rules governing the process are being adopted today.[1311]

According to filings made with the Commission, from 2009 to 2014, there were approximately 4,559 issuers per year in new Regulation D offerings with offer sizes of up to $1 million (excluding issuers that are pooled investment vehicles), including approximately 1,020 (22%) per year that reported having no revenue and approximately 861 (19%) per year that reported revenues of up to $1 million.[1312] Among issuers in new Regulation D offerings with offer sizes of up to $1 million (excluding issuers that are pooled investment vehicles) during this period, the overwhelming majority of issuers (approximately 80%) are younger than 5 years old,

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1311 *See also* Section IV.B.1.

1312 In addition, in an average year, approximately 50% of issuers in new Regulation D offerings with offer sizes of up to $1 million (excluding issuers that are pooled investment vehicles) declined to disclose their revenues. It is also possible that some issuers in Regulation D offerings that report revenues in excess of $1 million may participate in offerings in reliance on Section 4(a)(6).

with the median age of approximately one year. Approximately 92% of these issuers were organized as either a corporation or a limited liability company.

It is expected that many future issuers of securities in crowdfunding offerings would have otherwise raised capital from one of the alternative sources of financing discussed above, while others would have been financed by friends and family or not financed at all. Due to the differences between small business loans (including SBA-guaranteed loans) and securities-based crowdfunding offerings that can be conducted under the final rules, we are not able to estimate how many small businesses utilizing these forms of financing may instead pursue an offering in reliance on Section 4(a)(6). Similarly, due to the differences between the terms of crowdfunding campaigns in existence today and the provisions of the final rules, is not clear how many current campaigns can instead become offerings in reliance on Section 4(a)(6).[1313] Hence, while some of the businesses using these alternative funding sources may become issuers offering and selling securities in reliance on Section 4(a)(6) in the future, we cannot know how many of these businesses will elect securities-based crowdfunding in reliance on Section 4(a)(6) once it becomes available, nor can we know how many future businesses may not be financed at all.

We believe that many potential issuers of securities through crowdfunding will be startups and small businesses that are close to the "idea" stage of the business venture and that have

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[1313] A recent industry report estimated that the equity-based crowdfunding volume in North America in 2014 was $787.5 million and the average size of a successful equity-based crowdfunding campaign was $175,000. *See* Massolution 2015 at 55 and 60. This allows us to estimate approximately 4,500 successful equity-based crowdfunding campaigns for North America in 2014. The report does not provide statistics for the United States alone. Equity-based crowdfunding campaigns in the United States are currently limited to accredited investors or intrastate offerings in certain jurisdictions. Further, the industry report does not provide information that would allow us to estimate the number of crowdfunding campaigns of other types (such as reward-based or donation-based) in North America or the United States in 2014. We note that many such campaigns, particularly those that relate to individual projects, may not have a defined or sustained business model commensurate with typical issuers of securities. In particular, many of the current reward-based or donation-based crowdfunding projects likely entail endeavors that may not be suitable to a long-lived securities issuance (*e.g.*, certain artistic endeavors or artistic projects).

business plans that are not sufficiently well-developed or do not offer the growth potential or business model to attract VCs or angel investors. In this regard, a study of one large platform revealed that relatively few companies on that platform operate in technology sectors that typically attract VC investment activity.[1314]

b. Intermediaries

Section 4(a)(6)(C) requires that an offer and sale of securities in reliance on Section 4(a)(6) be conducted through a registered funding portal or a broker. Registered broker-dealers, both those that are already registered with the Commission and those that will register, might wish to facilitate securities-based crowdfunding transactions. New entrants that do not wish to register as broker-dealers might decide to register as funding portals to facilitate securities-based crowdfunding transactions in reliance on Section 4(a)(6). Donation-based or reward-based crowdfunding platforms with established customer relationships might seek to leverage these relationships and register as funding portals, or register as or associate with registered broker-dealers. Although the number of potential intermediaries that will fill these roles is uncertain, practices of existing broker-dealers and crowdfunding platforms provide insight into how the market might develop.

Based on FOCUS Reports filed with the Commission, as of December 2014, there were 4,267 broker-dealers registered with the Commission, with average total assets of approximately $1.1 billion per broker-dealer. The aggregate total assets of these registered broker-dealers are approximately $4.9 trillion. Of these registered broker-dealers, 816 also are dually registered as investment advisers.

[1314] *See* Ethan R. Mollick, *The Dynamics of Crowdfunding: An Exploratory Study*, Working Paper (June 26, 2013), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2088298.

Existing crowdfunding platforms are diverse and actively involved in financing, allowing thousands of projects to search for capital. A recent industry report estimates that, as of 2014, 1,250 crowdfunding platforms were operating worldwide, including 375 platforms operating in North America.[1315] Globally, approximately 19% (236) of platforms were engaged in equity-based crowdfunding, 18.3% in lending-based crowdfunding, 22.6% in donation-based crowdfunding, 28.9% in reward-based crowdfunding, with the remainder engaged in royalty-based and hybrid crowdfunding.[1316] An earlier industry report indicated that crowdfunding platforms typically charge entrepreneurs a "transaction fee" that is based on how large the target amount is and/or upon reaching the target and that fees from survey participants worldwide ranged from 2% to 25%, with an average of 7% in North America and Europe.[1317] The 2012 industry report provides one case study of fees for a "large-securities-based CFP" stating "[t]here are no management fees for uncommitted capital, but a "2 and 20" arrangement is set on deals funded."[1318]

We do not know at present which market participants will become intermediaries under Section 4(a)(6) and Regulation Crowdfunding, but we believe that existing crowdfunding platforms might seek to leverage their already-existing Internet-based platforms, brand recognition and user bases to facilitate offerings in reliance on Section 4(a)(6).[1319]

1315 *See* Massolution 2015 at 84. The report does not provide separate statistics for the United States.

1316 *Id.* at 89.

1317 *See* Massolution *Crowdfunding Industry Report: Market Trends, Composition and Crowdfunding Platforms* (May 2012) ("Massolution 2012") at 38.

1318 *Id.*

1319 For example, the Massolution 2012 industry report suggests that funding portal reputation is important in the crowdfunding market, especially for equity-based crowdfunding. *See* Massolution 2012 at 46.

Under the statute and the final rules, funding portals are constrained in the services they can provide, and persons (or entities) seeking the ability to participate in activities unavailable to funding portals, such as offering investment advice or holding, managing, possessing or otherwise handling investor funds, would instead need to register as broker-dealers or investment advisers, depending on their activities. Although we expect that initially, upon adoption of the final rules, more new registrants will register as funding portals than as broker-dealers given the less extensive regulatory requirements imposed on funding portals, it is possible that market competition to offer broker-dealer services as part of intermediaries' service capabilities might either drive more broker-dealer growth in the longer term or provide registered funding portals with the incentive to form long-term partnerships with registered broker-dealers. One commenter suggested that funding portals may find it beneficial to cooperate with registered broker-dealers and transfer agents.[1320] Other commenters on the proposal did not provide additional information on this issue. There is anecdotal evidence that such partnerships are already forming under existing regulations in crowdfunding transactions involving accredited investors.[1321] The final rules provide that intermediaries will be deemed to have satisfied the requirement to have a

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1320 *See* TinyCat Letter (but noting that such partnerships should be optional).

1321 *See* David Drake, *Rich Man's Crowd Funding*, FORBES, Jan. 15, 2013, *available at* http://www.forbes.com/sites/groupthink/2013/01/15/rich-mans-crowd-funding/. *See also* Mohana Ravindranath, *For broker/dealers, crowdfunding presents new opportunity*, WASH. POST, Mar. 29, 2013, *available at* http://www.washingtonpost.com/business/on-small-business/for-brokerdealers-crowdfunding-presents-new-opportunity/2013/03/28/bb835942-8075-11e2-8074-b26a871b165a_story.html; J.J. Colao, *In the Crowdfunding Gold Rush, This Company Has a Rare Edge*, FORBES, June 5, 2013, *available at* http://www.forbes.com/sites/jjcolao/2013/06/05/in-the-crowdfunding-gold-rush-this-company-has-a-rare-edge/; Arina Shulga, *Crowdfunding Right Now (Fund Model, Broker-Dealer Model, Lending Platforms and Intrastate Offerings)*, LEXISNEXIS.COM, Aug. 7, 2014, *available at* http://www.lexisnexis.com/legalnewsroom/banking/b/venture-capital/archive/2014/08/07/crowdfunding-right-now-fund-model-broker-dealer-model-lending-platforms-and-intrastate-offerings.aspx; Alessandra Malito, *Broker-dealer expands crowdfunding reach with new partnership*, INVESTMENTNEWS, Apr. 14, 2015, *available* at http://www.investmentnews.com/article/20150414/FREE/150419972/broker-dealer-expands-crowdfunding-reach-with-new-partnership.

reasonable basis for believing that an issuer has established means to keep accurate records of the holders of the securities it would offer and sell through the intermediary's platform if the issuer has engaged the services of a registered transfer agent.[1322] This registered transfer agent safe harbor may lead intermediaries to encourage issuers to use a registered transfer agent.

c. Investors

It is unclear what types of investors will participate in offerings made in reliance on Section 4(a)(6), but given the investment limitations in the final rules, we believe that many investors affected by the final rules will likely be individual retail investors who currently do not have broad access to investment opportunities in early-stage ventures. Offerings made in reliance on Section 4(a)(6) may provide retail investors with additional investment opportunities, although the extent to which they invest in such offerings will likely depend on their view of the potential return on investment as well as the risk for fraud.

In contrast, larger, more sophisticated or well-funded investors may be less likely to invest in offerings made in reliance on Section 4(a)(6). The relatively low investment limits set by the statute for crowdfunding investors may make these offerings less attractive for professional investors, including VCs and angel investors.[1323] While an offering made in reliance on Section 4(a)(6) can bring an issuer to the attention of these investors, it is possible that professional investors will prefer, instead, to invest in offerings in reliance on Rule 506, which are not subject to the investment limitations applicable to offerings made in reliance on Section 4(a)(6).

1322 *See* Rule 301(b) of Regulation Crowdfunding.

1323 An observer suggests that, unlike angels, VCs may be less interested in crowdfunding because, if VCs rely on crowdfunding sites for their deal flow, it would be difficult to justify charging a 2% management fee and 20% carried interest to their limited partners. *See* Ryan Caldbeck, *Crowdfunding – Why Angels, Venture Capitalists And Private Equity Investors All May Benefit*, FORBES, Aug. 7, 2013.

d. Other Capital Providers, Broker-Dealers and Finders in Private Offerings

The final rules may affect other parties that provide sources of capital, such as small business lenders, VCs, family and friends and angel investors that currently finance small private businesses. The current scope of financing provided by these capital providers is discussed above. As discussed below, the magnitude of the final rules' economic impact will depend on whether crowdfunding in reliance on Section 4(a)(6) emerges as a substitute or a complement to these financing sources.

In addition, issuers conducting private offerings may, outside of offerings in reliance on Section 4(a)(6), currently use broker-dealers to help them with various aspects of the offering and to help ensure compliance with the ban on general solicitation and advertising that exists for most private offerings. Private offerings also could involve finders who connect issuers with investors for a fee.[1324] These private offering intermediaries also may be affected by the final rules, because once issuers can undertake offerings in reliance on Section 4(a)(6), some issuers might no longer need the services of those broker-dealers and finders.

Although we are unable to predict the exact size of the market for broker-dealers and finders in private offerings that are comparable to those that the final rules permit, data on the use of broker-dealers and finders in the Regulation D markets suggest that they may not currently play a large role in private offerings. Based on a staff study, only 21% of all new Regulation D offerings from 2009 to 2014 used an intermediary such as a broker-dealer or a finder.[1325] The use of a broker-dealer or a finder increased with offering size; they participated in approximately 17%

1324 Depending on their activities, these persons may need to be registered as broker-dealers.

1325 *See Unregistered Offerings White Paper*, note 1230.

of offerings for up to $1 million and 30% of offerings for more than $50 million. Moreover, the fee tends to decrease with offering size. Unlike the gross spreads in registered offerings, the differences in fees for Regulation D offerings of different sizes are large: the average total fee (commission plus finder fee) paid by issuers conducting offerings of up to $1 million (6.4% in 2014) is almost three times larger on a percentage basis than the average total fee paid by issuers conducting offerings of more than $50 million (1.9% in 2014).[1326] These estimates, however, only reflect practices in the Regulation D market. It is possible that issuers engaging in other types of private offerings (*e.g.*, those relying on Section 4(a)(2)), for which we do not have data, may use broker-dealers and finders more frequently and have different fee structures.

B. Analysis of Final Rules

As noted above, we are mindful of the costs and benefits of the final rules, as well as the impact that the final rules may have on efficiency, competition and capital formation. In enacting Title III, Congress established a framework for a new type of exempt offering and required us to adopt rules to implement that framework. To the extent that crowdfunding rules are successfully utilized, the crowdfunding provisions of the JOBS Act are expected to provide startups and small businesses with the means to raise relatively modest amounts of capital, from a broad cross section of investors, through securities offerings that are exempt from registration under the Securities Act. They also are expected to permit small investors to participate in a wider range of securities offerings than may be currently available.[1327] Specifically, the statutory provisions and the final rules address several challenges specific to financing startups and small businesses,

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1326 *Id.*

1327 *See, e.g.*, 158 CONG. REC. S1781 (daily ed. Mar. 19, 2012) (statement of Sen. Carl Levin) ("Right now, the rules generally prohibit a company from raising very small amounts from ordinary investors without significant costs.").

including, for example, accessing a large number of investors, the regulatory requirements associated with issuing a security, protecting investors and making such securities offerings cost-effective for the issuer.

In the sections below, we analyze the costs and benefits associated with the crowdfunding regulatory regime, as well as the potential impacts of such a regulatory regime on efficiency, competition and capital formation, in light of the baseline discussed above.

1. Broad Economic Considerations

In this release, we discuss the potential costs and benefits of the final rules. Many of these costs and benefits are difficult to quantify or estimate with any degree of certainty, especially considering that Section 4(a)(6) provides a new method for raising capital in the United States. Some costs are difficult to quantify or estimate because they represent transfers between various participants in a market that does not yet exist. For instance, costs to issuers can be passed on to investors and costs to intermediaries can be passed on to issuers and investors. These difficulties in estimating and quantifying such costs are exacerbated by the limited public data that indicates how issuers, intermediaries and investors will respond to these new capital raising opportunities.

The discussion below highlights several general areas where uncertainties about the new crowdfunding market might affect the potential costs and benefits of the final rules, as well as our ability to quantify those costs and benefits. It also highlights the potential effects on efficiency, competition and capital formation.

The extent to which the statute and the final rules affect capital formation and the cost of capital to issuers depends in part on the issuers that choose to participate. In particular, if offerings in reliance on Section 4(a)(6) only attract issuers that are otherwise able to raise capital through another type of exempt offering, the statute and the final rules may result in a

redistribution of capital flow, which may enhance allocative efficiency but have a limited impact on the aggregate level of capital formation.[1328]

Notwithstanding the existence of these alternative methods of capital raising, we believe that offerings pursuant to Section 4(a)(6) will likely represent a new source of capital for many small issuers that currently have difficulty raising capital. Startups and small businesses usually have smaller and more variable cash flows than larger, more established companies, and internal financing from their own business operations tends to be limited and unstable. Moreover, these businesses tend to have smaller asset bases[1329] and, thus, less collateral for traditional bank loans. As discussed above, startups and small businesses, which are widely viewed to have more financial constraints than publicly-traded companies and large private companies, could therefore benefit significantly from a securities-based crowdfunding market. Some small businesses may not qualify for traditional bank loans and may find alternative debt financing too costly or incompatible with their financing needs. While some small businesses may attract equity investments from angel investors or VCs, other small businesses, particularly, businesses at the seed stage may have difficulty obtaining external equity financing from these sources. We believe that the statute, as implemented by the final rules, may increase both capital formation and the efficiency of capital allocation among small issuers by expanding the range of methods of external financing available to small businesses and the pool of investors willing to finance such types of

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1328 For example, a 2012 GAO report on Regulation A offerings suggests that a significant decline in the use of this funding alternative after 1997 could be partially attributed to a shift to Rule 506 offerings under Regulation D, as a result of the preemption of state law registration requirements for Rule 506 offerings that occurred in 1996. *See* GAO Report, note 1231.

1329 *See, e.g.*, John Asker, Joan Farre-Mensa and Alexander Ljungqvist, *Corporate Investment and Stock Market Listing: A Puzzle?* European Corporate Governance Institute Finance Working Paper (June 2012), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1603484.

businesses. The extent to which such issuers will use the Section 4(a)(6) offering exemption, however, is difficult to assess.

If startups and small businesses find other capital raising options more attractive than securities-based crowdfunding, the impact of Section 4(a)(6) on capital formation may be limited. Even so, the availability of securities-based crowdfunding as a financing option may increase competition among suppliers of capital, resulting in a potentially lower cost of capital for all issuers, including those that choose not to use securities-based crowdfunding.

For issuers that pursue offerings in reliance on Section 4(a)(6), establishing an initial offering price might be challenging. Offerings relying on Section 4(a)(6) will not involve an underwriter who, for larger offerings, typically assists the issuer with pricing and placing the offering. Investors in offerings relying on Section 4(a)(6) may lack the sophistication to evaluate the offering price. Thus, the involvement of these investors, who are likely to have a more limited capacity for conducting due diligence on deals, may contribute to less accurate valuations.

Moreover, because of the investment limitations in securities-based crowdfunding transactions, there may not be a strong incentive, even assuming adequate knowledge and experience, for an investor to perform a thorough analysis of the issuer disclosures. To the extent that these potential information asymmetries resulting from the lack of a thorough analysis of the disclosures are anticipated by prospective investors, investor participation in offerings made in reliance on Section 4(a)(6) may decline and the associated benefits of capital formation may be lower.

Uncertainty surrounding exit strategies for investors in crowdfunding offerings also may limit the benefits. In particular, it is unlikely that purchasers in crowdfunding transactions will be able to follow the typical path to liquidity that investors in other exempt offerings follow. For

instance, investors in a VC-backed startup may eventually sell their securities in an initial public offering on a national securities exchange or to another company in an acquisition.[1330] We anticipate that most businesses engaging in offerings in reliance on Section 4(a)(6) will be unlikely to progress directly to an initial public offering on a national securities exchange given their small size,[1331] and investors may lack adequate strategies or opportunities to eventually divest their holdings.[1332] A sale of the business will require the issuer to have a track record in order to attract investors with the capital willing to buy the business.

Further, the likely broad geographical dispersion of crowdfunding investors may make shareholder coordination difficult. It may also exacerbate information asymmetries between issuers and investors, if the distance between them diminishes the ability for investors to capitalize on local knowledge that may be of value in assessing the viability of the issuer's business. The use of electronic means may mitigate some of these difficulties. Even if an issuer can execute a sale or otherwise offer to buy back or retire the securities, it might be difficult for investors to determine whether the issuer is offering a fair market price. These uncertainties may limit the use of the Section 4(a)(6) exemption.

The potential benefits of the final rules also may depend on how investors respond to potential liquidity issues unique to the securities-based crowdfunding market. It is currently unclear how securities offered and sold in transactions conducted in reliance on Section 4(a)(6)

1330 *See* Gompers, note 1249.

1331 As noted, under the statute and the final rules, issuers relying on Section 4(a)(6) would be limited to raising an aggregate of $1 million during a 12-month period. By contrast, as noted in the IPO Task Force, the size of an initial public offering generally exceeds $50 million. *See* IPO Task Force, note 1223.

1332 In contrast, given the required investor qualifications and offering limit amounts, Regulation D offerings may generally attract issuers that are more experienced and better capitalized. Moreover, such offerings are likely to have a larger proportion of accredited investors because, in contrast to securities-based crowdfunding, there are no limitations on individual investment amounts. As a result, we believe that Regulation D issuers and investors are more likely to have potential exit strategies in place.

will be transferred in the secondary market after the one-year restricted period ends, and investors who purchased securities in transactions conducted in reliance on Section 4(a)(6) and who seek to divest their securities may not find a liquid market.[1333] Assuming a secondary market develops, securities may be quoted on the over-the-counter market or on trading platforms for shares of private companies.[1334] Nevertheless, it is possible that secondary trading costs for investors may be substantial, effective and quoted spreads may be wide, trading volume may be low, and price volatility may be high compared to those of listed securities.[1335] Illiquidity, to different degrees, remains a concern for other exempt offerings and for registered offerings by small issuers. However, because investors purchasing securities sold in reliance on Section 4(a)(6) may be less sophisticated than investors in other private offerings due to the fact that there are no investor qualification requirements, they may face additional challenges in addressing the impact of illiquidity, either in finding a suitable trading venue or negotiating with the issuer for an alternative liquidity option. The potentially high degree of illiquidity associated with securities

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1333 Academic studies have shown that the over-the-counter market is less liquid than the national exchanges. *See* Nicolas Bollen and William Christie, *Market Microstructure of the Pink Sheets*, 33 J. BANKING & FIN. 1326–1339 (2009); Andrew Ang, Assaf Shtauber and Paul Tetlock, *Asset Pricing in the Dark: The Cross Section of OTC Stocks*, 26 REV. FIN. STUD. 2985–3028 (2013).

1334 Given the services that funding portals are permitted to provide under the statute and the final rules, investors will not be able to use funding portals to trade in securities offered and sold in reliance on Section 4(a)(6) in the secondary market.

1335 Academic studies show that reducing the information transparency about an issuer increases the effective and quoted spreads of its shares, reduces share price and increases price volatility. Specifically, percentage spreads triple and volatility doubles when NYSE issuers are delisted to the Pink Sheets. *See* Jonathan Macey, Maureen O'Hara and David Pompilio, *Down and Out in the Stock Market: The Law and Finance of the Delisting Process*, 51 J.L. & ECON 683–713 (2008). When NASDAQ issuers delist and subsequently trade on the OTC Bulletin Board and/or the Pink Sheets, share volume declines by two-thirds, quoted spreads more than double, effective spreads triple and volatility triples. *See* Jeffrey H. Harris, Venkatesh Panchapagesan and Ingrid M. Werner, *Off But Not Gone: A Study of NASDAQ Delistings*, Fisher College of Business Working Paper No. 2008-03-005 and Dice Center Working Paper No. 2008-6 (Mar. 4, 2008), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=628203. One factor that may alleviate transparency concerns is the fact that issuers that sold securities in an offering made in reliance on Section 4(a)(6) will have an ongoing reporting obligation, so disclosure of information about the issuer will continue to be required.

purchased in reliance on Section 4(a)(6) may discourage some investors from investing in issuers through such offerings, thus limiting the potential efficiency, competition and capital formation benefits of the final rules.

Even with the mandated disclosures, unsophisticated investors purchasing securities issued in reliance on Section 4(a)(6) may face certain expropriation risks, potentially limiting the upside of their investment, even when they select investments in successful ventures. This can occur if issued securities include certain features (*e.g.*, callable securities or securities with differential control rights) or if issuers conduct insider-only financing rounds or financing rounds at reduced prices (so-called "down rounds") that have the effect of diluting an investor's interest or otherwise diminishing the value of the securities offered and sold in reliance on Section 4(a)(6). Investors purchasing securities issued in reliance on Section 4(a)(6) may not have the experience or the market power to negotiate various anti-dilution provisions, right of first refusal, tag-along rights, superior liquidation preferences and rights upon a change in control that have been developed by institutional and angel investors as protections against fundamental changes in a business.[1336] Moreover, the disperse ownership stakes of investors in securities-based crowdfunding offerings may weaken their incentives to monitor the issuer to minimize the risk of expropriation. The ensuing expropriation risk may discourage some investors from participating in offerings made in reliance on Section 4(a)(6), potentially limiting the efficiency, competition and capital formation benefits of the final rules.

The final rules also may have an effect on broker-dealers and finders participating in private offerings. Some issuers that previously relied on broker-dealers and finders to assist with raising capital through private offerings may, instead, begin to rely on the Section 4(a)(6)

[1336] *See* Kaplan, note 1279.

exemption to find investors. The precise impact of the final rules on these intermediaries will depend on whether (and, if so, to what extent) issuers switch from using existing exemptions to using the exemption provided by Section 4(a)(6) or whether the final rules primarily attract new issuers. The impact of the final rules on registered broker-dealers will also depend on the extent to which broker-dealers participate as intermediaries in the securities-based crowdfunding market. If a significant number of issuers switch from raising capital under existing private offering exemptions to relying on the exemption provided by Section 4(a)(6), this may negatively affect the revenue of finders and broker-dealers in the private offerings market. While this may disadvantage existing private offering market intermediaries, the new competition may ultimately lead to more efficient allocation of capital.

If securities-based crowdfunding primarily attracts new issuers to the market, the impact on broker-dealers and finder revenue may be negligible and the final rules may even have a positive effect on their revenues by revealing more potential clients for them, particularly to the extent that they chose to operate a funding portal. Additionally, greater investor interest in private company investment may increase capital formation, creating new opportunities for broker-dealers and finders that otherwise would have been unavailable.

The final rules also may encourage current participants in the crowdfunding market to diversify their funding models to attract a broader group of companies and to provide additional investment opportunities for investors. For example, donation-based crowdfunding platforms that currently offer investment opportunities in micro-loans generally do not permit donors to collect interest on their investments because of concerns that this activity will implicate the federal

securities laws unless an exemption from registration is available.[1337] Under the final rules, these platforms may choose to register as funding portals and permit businesses to offer securities that provide investors with the opportunity to obtain a return on investment. This can broaden their user base and attract a group of investors different from those already participating in reward-based or donation-based crowdfunding. It is likely that some registered broker-dealers will find it profitable to enter the securities-based crowdfunding market and operate funding portals as well. Such an entry will increase the competition among intermediaries and likely lead to lower issuance costs for issuers.

However, many projects that are well suited for reward-based or donation-based crowdfunding (*e.g.*, because they have finite lives, their payoffs to investors could come before the project is completed or could be contingent on the project's success, etc.) may have little in common with startups and small businesses that are well suited for an offering in reliance on Section 4(a)(6). As a result, diversification among existing platforms may not always be optimal or preferred, particularly if complying with the final rules proves disproportionately costly compared to the potential amount of capital to be raised.

2. Crowdfunding Exemption

a. Limitation on Capital Raised

The statute imposes certain limitations on the total amount of securities that may be sold by an issuer during the 12-month period preceding the date of the transaction made in reliance on Section 4(a)(6). Specifically, Section 4(a)(6)(A) provides for a maximum aggregate amount of $1 million sold in reliance on the exemption during a 12-month period.[1338] The final rules preserve

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1337 *See, e.g.*, *Deutsche Bank Microcredit Development Fund, Inc.*, SEC No-Action Letter (Apr. 8, 2012).

1338 *See also* Rule 100(a)(1) of Regulation Crowdfunding.

the $1 million limit. The limitation on the amount that may be raised is expected to benefit investors by reducing the potential loss from dilution or fraud[1339] in the securities-based crowdfunding market. However, we recognize that this limit on the amount that may be sold in reliance on Section 4(a)(6) also can prevent certain issuers from raising all the capital they need to make their businesses viable, which in turn can result in lost opportunities, as indicated by various commenters.[1340] It also is likely to limit efficiency to the extent that capital cannot be channeled to the most productive use. Due to the lack of data, however, we are not able to quantify the unrealized efficiency or capital formation associated with the adoption of the $1 million limit instead of the alternative of a higher limit. Since issuers in securities-based crowdfunding offerings bear certain fixed costs, as discussed in Section III.B.3., offering costs as a percentage of offering proceeds will be larger under the $1 million limit than under the alternative of a higher limit.

As an alternative, we could have defined the $1 million limit to be net of intermediary fees, as suggested by some commenters.[1341] If a funding portal announces in advance the fees it

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1339 While we lack information to predict the potential incidence of fraud in securities-based crowdfunding offerings made in reliance on Section 4(a)(6) and note that current crowdfunding practices differ significantly from the securities-based crowdfunding market that may develop upon effectiveness of the final rules, some concern has been expressed about the potential for fraud in this area. *See, e.g.*, NASAA Enforcement Report: 2015 Report on 2014 data, September 2015, available at http://nasaa.cdn.s3.amazonaws.com/wp-content/uploads/2011/08/2015-Enforcement-Report-on-2014-Data_FINAL.pdf (listing Internet fraud (including social media and crowdfunding) among the products and schemes that are frequently investigated by states, without statistics specific to securities-based crowdfunding).

1340 *See, e.g.*, Advanced Hydro Letter; Bushroe Letter; Cole D. Letter; Concerned Capital Letter; Hamman Letter; Harrison Letter; Hillside Letter; Jazz Letter; Kickstarter Coaching Letter; McCulley Letter; McGladrey Letter; Meling Letter; Miami Nation Enterprises Letter; Multistate Tax Service Letter; Peers Letter; Pioneer Realty Letter; Public Startup Letter 2; Qizilbash Letter; Rosenthal O. Letter; Sarles Letter; SBM Letter; Taylor R. Letter; Taylor T. Letter; Wales Capital Letter 1; Wales Capital Letter 3; WealthForge Letter; Wear Letter; Wilhelm Letter; Winters Letter; Yudek Letter.

1341 *See, e.g.*, Benjamin Letter; FundHub Letter 1; Hackers/Founders Letter; Joinvestor Letter; Odhner Letter; Omara Letter; Public Startup Letter 2; RFPIA Letter; RoC Letter; RocketHub Letter; Seed&Spark Letter; Thomas Letter 1; Wales Capital Letter 1; Whitaker Chalk Letter; Wilson Letter.

charges for a given transaction (fixed or variable), the economic effects of such an alternative definition would be qualitatively similar to the effects of raising the offering limit. If the funding portal fees are not known in advance, then this alternative may also create uncertainty for issuers about how much capital they would be able to raise. Several commenters opposed such an alternative.[1342]

The costs associated with not increasing the investment limit above $1 million are mitigated in part by the ability of issuers to concurrently seek additional financing in reliance on another type of exempt offering, such as Regulation D or Regulation A, in addition to the offering in reliance on Section 4(a)(6). In this release, we provide guidance clarifying our view that issuers may conduct other exempt offerings without having those offerings integrated with the offering made in reliance on Section 4(a)(6), provided that each offering complies with the applicable exemption relied upon for that particular offering. Several commenters opposed this approach on the ground that it could result in fewer investor protections than if the offerings were integrated. Some commenters noted that a potential cost to investors associated with not requiring integration is a reduction in investor protection due to the possibility of an issuer's use of advertising for one offering to indirectly promote another exempt offering that would have been subject to more stringent advertising restrictions.[1343] While we recognize this concern, we note that the final rules do not provide a blanket exemption from integration with other private offerings that are conducted simultaneously with, or around the same time as, a Section 4(a)(6) offering. Rather, we provide guidance that an offering made in reliance on Section 4(a)(6) is not required to be

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1342 *See, e.g.*, Arctic Island Letter 4; ASSOB Letter; Commonwealth of Massachusetts Letter; MCS Letter; PeoplePowerFund Letter.

1343 *See* AFR Letter; BetterInvesting Letter; Consumer Federation Letter; Fund Democracy Letter; IAC Recommendation; MCS Letter.

integrated with another exempt offering made by the issuer to the extent that each offering complies with the requirements of the applicable exemption that is being relied upon for that particular offering. As mentioned earlier, an issuer conducting a concurrent exempt offering for which general solicitation is not permitted will need to be satisfied that purchasers in that offering were not solicited by means of the offering made in reliance on Section 4(a)(6). Alternatively, an issuer conducting a concurrent exempt offering for which general solicitation is permitted, for example, under Rule 506(c), cannot include in any such general solicitation an advertisement of the terms of an offering made in reliance on Section 4(a)(6), unless that advertisement otherwise complies with Section 4(a)(6) and the final rules. This may partly alleviate some of commenters' concerns because each offering will have the investor protections of the offering exemption upon which it relies.

As an alternative, in line with the suggestions of some commenters,[1344] we could have provided guidance that the amounts offered in reliance on Section 4(a)(6) should be integrated with the amounts offered pursuant to other exempt offerings. Under such an alternative, the amounts raised in other exempt offerings would count toward the maximum offering amount under Section 4(a)(6). Such an alternative would potentially limit the amount of capital raised by issuers, including the set of issuers eligible to conduct an exempt offering relying on Section 4(a)(6), and thus potentially limit the capital formation benefits of the final rules. Compared to this alternative, the ability of issuers to conduct other exempt offerings that do not count toward the maximum offering amount under Section 4(a)(6) may alleviate some of the concerns that certain issuers will not be able to raise sufficient capital. The net effect on capital

[1344] *See, e.g.*, AFL-CIO Letter; Brown J. Letter; Consumer Federation Letter; Fund Democracy Letter; MCS Letter; NASAA Letter.

formation will also depend on whether issuers seeking an aggregate exempt offering amount in excess of $1 million elect to rely on Regulation Crowdfunding as part of their capital raising or elect to rely on a different exemption, such as Rule 506 of Regulation D. These considerations and the relative differences in the investor protections associated with the different offering exemptions will determine the net effect on the amount of information about issuers available to market participants and the level of investor protection.

b. Investment Limitations

Since offering documents for offerings made in reliance on Section 4(a)(6) will not be subject to review by Commission staff prior to the sale of securities, we are sensitive to potential investor protection concerns arising from the participation of less sophisticated investors in these exempt offerings. Some commenters[1345] raised concerns that the "wisdom of the crowd" will not result in investors pooling information so as to lead to better informed investment decisions.[1346]

1345 *See, e.g.*, AFR Letter; Brown J. Letter; Consumer Federation Letter.

1346 Predictions in research studies regarding the impact of social interaction on investor decisions are mixed. On the one hand, a recent study of opinions that were posted on the Internet website http://seekingalpha.com finds evidence of predictability of earnings surprises and returns that is interpreted as potentially suggesting the value relevance of user opinions rather than a naïve investor reaction. *See* Hailiang Chen, Prabuddha de, Yu Hu, and Byoung-Hyoun Hwang, *Wisdom of Crowds: The Value of Stock Opinions Transmitted Through Social Media*, 27 REV. FIN. STUD. 1367–1403 (2014). An earlier theoretical paper shows that word-of-mouth can, under some circumstances, result in superior decisions. *See* Glenn Ellison and Drew Fudenberg, *Word-of-Mouth Communication and Social Learning*, 110 QUARTERLY J. ECON. 93–125 (1995). On the other hand, some behavioral finance literature examines irrational herding and contagion of thought and behavior through social interaction, such as the propagation of investing memes, which need not be predictive of superior trading performance. For example, one article characterizes memes as "mental representation (such as an idea, proposition, or catchphrase) that can be passed from person to person". The article provides an example of investors using "verbal 'reasons' to decide how to trade" and notes that these reasons "are often not cogent". The article notes that such reasons, or financial memes, can be simple or can be elaborate structures of analysis, examples, terminology, catchphrases, and modeling. *See* for example, David A. Hirshleifer and Siew Hong Teoh, *Thought and Behavior Contagion in Capital Markets*, HANDBOOK OF FINANCIAL MARKETS: DYNAMICS AND EVOLUTION (2009). Another article compares the investment decisions of stock clubs and individuals. It finds that while both individuals and clubs are more likely to purchase stocks that are associated with "good reasons" (such as a company that is featured on a list of "most-admired" companies), stock clubs favor such stocks more than individuals, despite the fact that such reasons do not improve performance. The article analyzes social dynamics that may make "good reasons" more important for groups than individuals. *See* Brad Barber, Chip Heath, and Terrance Odean, *Good*

While we acknowledge these concerns, we note that, by adding Section 4(a)(6) to the Securities Act, Congress made an express determination to facilitate securities-based crowdfunding transactions under the federal securities laws, subject to certain specified investor protections.

Consistent with the statute, the final rules incorporate several important investor protections, including limits on the amount that can be raised, issuer eligibility criteria, and issuer and intermediary requirements, including statutorily mandated investor education requirements. The statute and the final rules also impose certain limitations on the aggregate dollar amount of securities in offerings in reliance on Section 4(a)(6) that may be sold to an investor during a 12-month period.[1347] These provisions are designed to limit the potential investment and, consequently, the potential losses for any single investor, thus providing downside protection for investors.

We recognize that these provisions also will limit the potential upside for investors. This may particularly affect the decisions of investors with large portfolios who might be able to absorb losses and understand the risks associated with risky investments and who may have more expertise and stronger incentives to acquire and analyze information about an issuer. For these investors, the $100,000 aggregate limit may reduce their incentive to participate in the securities-based crowdfunding market, compared to other types of investments, potentially depriving the securities-based crowdfunding market of more experienced and knowledgeable investors and impeding capital formation. Moreover, limiting the participation of such investors may negatively affect the informational efficiency of the securities-based crowdfunding market because

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Reasons Sell: Reason-Based Choice Among Group and Individual Investors in the Stock Market, 49 MANAGEMENT SCIENCE 1636–1652 (2003).

[1347] *See* Section 4(a)(6)(B). *See also* Rule 100(a)(2) of Regulation Crowdfunding.

sophisticated investors are better able to accurately price such offerings. These investors also can add value to the discussions taking place through an intermediary's communication channels about a potential offering by providing their views on the issuer's financial viability and potential for fraud. Persons with larger portfolios are also likely to be in a better position to monitor the issuer's insiders, which can reduce the extent of moral hazard and the risk of fraud on the part of the issuer and the issuer's insiders, yielding benefits for all investors. Such investors also can add value by advising the issuer and contributing strategic expertise, which can be particularly beneficial for early-stage issuers. Some of these potential benefits, however, may still be available to issuers that seek to attract such investors through another type of exempt offering, such as a Regulation D offering.

The aggregate limit on crowdfunding investments also can impede the ability of investors to diversify within the securities-based crowdfunding market. As securities-based crowdfunding investments might have inherently high failure rates,[1348] investors who do not or cannot diversify their investments across a number of offerings can face an increased risk of incurring large losses, relative to their investments, even when they investigate offerings thoroughly. By comparison, VC firms typically construct highly diversified portfolios with the understanding that many ventures fail, resulting in a complete loss of some investments, but with the expectation that those losses will be offset by the large upside of the relatively fewer investments that succeed.[1349] The securities-based crowdfunding market is expected to involve earlier-stage financing compared to venture capital financing, and therefore, the chances of investment success may be lower.[1350] The

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1348 *See* discussion in Section III.A.4 above.

1349 *See*, e.g., John Cochrane, *The Risk and Return of Venture Capital*, 75 J. OF FIN. ECON. 3 (2005).

1350 *See* Rajshree Agarwal and Michael Gort, *Firm and Product Life Cycles and Firm Survival*, 92 AM. ECON. REV. 184−190 (2002)

statutory caps on aggregate securities-based crowdfunding investments under Section 4(a)(6) may limit an investor's ability to choose a sufficiently large number of investments to offset this risk and to recover the due diligence costs of sufficiently investigating individual investments. One potential solution to this diversification problem is to invest smaller amounts in a greater number of ventures. However, such a strategy has limited benefit to the extent that there is a fixed cost to the due diligence associated with identifying and reviewing each investment opportunity, making it more costly to implement than a strategy that relies on the selection of fewer investment opportunities.

In a change from the proposed rules, both the investor's annual income and net worth must be above $100,000 for the 10 percent limitation to apply. This change is intended to strengthen investor protections for investors whose annual income or net worth is below $100,000. Such investors may not be as well situated to bear the risk of loss (*e.g.*, in the event of fraud on the part of an issuer) as investors with both income and net worth of $100,000 or more. According to Commission staff analysis of the data in the 2013 Survey of Consumer Finances, approximately 17% of U.S. households have both income and net worth of $100,000 or higher. By comparison, 39% of U.S. households have either income or net worth of $100,000 or higher.[1351] Thus, approximately 22% of households will be subject to a lower investment limit under the final rules than under the proposal. We note that these figures are only available at the household level rather than at the individual level. We further note that these figures do not account for the fact that only some households might seek to invest in an offering in reliance on Section 4(a)(6).

[1351] Based on data from the 2013 Survey of Consumer Finances, a triennial survey sponsored by the Federal Reserve Board, *available* at http://www.federalreserve.gov/econresdata/scf/scfindex.htm.

Thus, we are not able to determine the actual percentage of investors affected by this change in the final rules relative to the proposal.

Within each investment limitation tier, the investment limitation percentage is multiplied by the "lesser of" an investor's annual income or net worth in the investment limitation calculation, which was suggested by several commenters.[1352] This change from the proposal is expected to reduce the permitted investment limit for each individual investor because most investors are unlikely to have annual income and net worth amounts that are identical.[1353]

Investment limitations will likely have a negative effect on capital formation. For example, investment limitations may make it more difficult for some issuers to reach their funding targets. However, these limits also are expected to reduce the risk and impact of potential loss for investors that accompany the high failure rates associated with investments in small businesses and startups, thus potentially improving investor protection. There is no available market data that would allow us to empirically evaluate the magnitude of these effects.

Consistent with the proposed rules, the final rules allow an issuer to rely on the efforts that an intermediary is required to undertake in order to determine that the aggregate amount of securities purchased by an investor will not cause the investor to exceed the investor limits, provided that the issuer does not have knowledge that the investor had exceeded, or would exceed, the investor limits as a result of purchasing securities in the issuer's offering, which was supported

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1352 *See, e.g.*, AFR Letter; BetterInvesting Letter; Consumer Federation Letter; Fund Democracy Letter; Fryer Letter; Growthfountain Letter; IAC Recommendation (but also stating that the "greater of" approach would be appropriate for accredited investors); Merkley Letter; NASAA Letter; Schwartz Letter; Zhang Letter (recommending that net worth not be used to calculate the investment limit).

1353 Although we lack information to determine the average change in the applicable investment limit resulting from this change, based on Commission staff analysis of the 2013 Survey of Consumer Finances, a larger percentage of households exceeded a particular dollar threshold, such as $100,000 or $200,000, based on the net worth standard than the percentage of households that exceeded the same dollar threshold based on the income standard.

by various commenters.[1354] This may result in aggregate verification cost savings since a given intermediary may be involved in and have information on crowdfunding transactions pertaining to the offerings of multiple issuers, which makes it potentially less costly to identify investors that exceed the investment limitation. As a potential alternative, we could have imposed more extensive verification requirements on issuers, which would have resulted in larger compliance costs for issuers but could have potentially increased investor compliance with the investment limitations, with corresponding investor protection benefits. As noted above, we believe the final rules appropriately consider investor protection and facilitating capital formation.

c. Issuer Eligibility

Section 4A(f) of the statute excludes certain categories of issuers from eligibility to engage in securities-based crowdfunding transactions in reliance on Section 4(a)(6). The final rules exclude those categories of issuers.[1355] The final rules also exclude two additional categories of issuers, beyond those identified in the statute, from being eligible to rely on Section 4(a)(6) to engage in crowdfunding transactions. First, the final rules exclude issuers that sold securities in reliance on Section 4(a)(6) and have not filed with the Commission and provided to investors the ongoing annual reports required by Regulation Crowdfunding during the two years immediately preceding the filing of the required offering statement,[1356] which is generally consistent with

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1354 *See, e.g.,* Arctic Island Letter 4; CFA Institute Letter; Consumer Federation Letter; CrowdBouncer Letter; EarlyShares Letter; EMKF Letter; Finkelstein Letter; Fund Democracy Letter; Heritage Letter; Joinvestor Letter; Public Startup Letter 2; RoC Letter; RocketHub Letter; Vann Letter; Wefunder Letter; Whitaker Chalk Letter.

1355 These categories of issuers are: (1) issuers that are not organized under the laws of a state or territory of the United States or the District of Columbia; (2) issuers that are subject to Exchange Act reporting requirements; (3) investment companies as defined in the Investment Company Act or companies that are excluded from the definition of investment company under Section 3(b) or 3(c) of the Investment Company Act. *See* Section 4A(f). *See also* Rule 100(b) of Regulation Crowdfunding.

1356 *See* discussion in Section II.A.4 above.

suggestions from several commenters.[1357] This additional exclusion is not expected to impose any additional burdens and costs on an issuer that it would not have already incurred had it complied with the ongoing reporting requirements as they came due. Further, the requirement that a delinquent issuer prepare and file up to two annual reports at one time in order to become eligible to rely on Section 4(a)(6) is expected to incentivize issuers to provide updated and current information to investors, if they intend to rely again on Section 4(a)(6) to raise additional capital, without necessarily requiring an issuer to become fully current in its reporting obligations. We recognize that conditioning an issuer's Section 4(a)(6) eligibility on the requirement that issuers provide ongoing reports for only the previous two years may result in less information being available to investors in some periods, with potential adverse effects on the price formation and liquidity of the securities in the secondary market. The potential damage to an issuer's reputation resulting from being delinquent along with potential enforcement action for failure to comply with a regulatory reporting obligation and the modification from the proposed rules to require an issuer to disclose in its offering statement if it or any of its predecessors previously failed to comply with the ongoing reporting requirements of Rule 203 of Regulation Crowdfunding, however, may help to mitigate these potential adverse effects. As an alternative, we could have chosen not to impose this exclusion or adopted a shorter look-back period, as suggested by some commenters.[1358] Compared to the provisions in the final rules, either of these alternatives could result in less information being available to investors and reduced informational efficiency of securities prices

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1357 *See, e.g.,* ASSOB Letter; Commonwealth of Massachusetts Letter; Consumer Federation Letter; Fund Democracy Letter; Grassi Letter; Joinvestor Letter; NASAA Letter; Wefunder Letter.

1358 *See, e.g.,* ABA Letter; Parsont Letter; Projectheureka Letter; Public Startup Letter 2; RocketHub Letter.

or possibly increased likelihood of issuer misconduct in offerings made in reliance on Section 4(a)(6).

Second, the final rules exclude a company that has no specific business plan or has indicated that its business plan is to engage in a merger or acquisition with an unidentified company or companies, as suggested by several commenters.[1359] This requirement is intended to help ensure that investors have adequate information about the issuer's proposed business plan to make an informed investment decision, which may increase investor protection in some instances. As an alternative, we could have chosen not to impose this exclusion or to impose a less restrictive exclusion, as suggested by several commenters.[1360] Although these alternatives might increase capital formation by allowing a subset of additional issuers to rely on Section 4(a)(6), they may also result in less informed investor decisions in such offerings.

Overall, categories of issuers that are excluded from eligibility under the final rules may be at a competitive disadvantage relative to those that are eligible to offer securities under the final rules, to the extent that excluded issuers may raise less external capital or incur a higher direct or indirect cost of financing, or additional restrictions, when seeking financing from alternative sources.

3. Issuer Requirements

a. Issuer Costs

We recognize that there are benefits and costs associated with Regulation Crowdfunding's requirements pertaining to issuers, including the final rule's disclosure requirements. In the

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1359 *See, e.g.*, Anonymous Letter 2; CFA Institute Letter; CFIRA Letter 7; Commonwealth of Massachusetts Letter; Consumer Federation Letter; NASAA Letter; ODS Letter; Traklight Letter; Whitaker Chalk Letter.

1360 S*ee, e.g.*, ABA Letter; FundHub Letter 1; Projectheureka Letter; Public Startup Letter 2; RoC Letter; RocketHub Letter; SBM Letter; Wilson Letter.

Proposing Release, we provided cost estimates for each of these requirements and requested comment on our estimates.[1361] In response, we received several comment letters providing alternative cost estimates, some of which were lower and some of which were higher than the cost estimates in the Proposing Release.[1362] For example, one commenter[1363] provided the following cost estimates: portal fees of 6% to 15%[1364]; accounting review fees of $1,950 to $9,000; accounting audit fees of $3,100 to $9,000; financial statements/projections costs of $2,000 to $5,000; Title III disclosure/compliance costs of $1,000 to $4,000; and corporate formation costs of $300 to $500.[1365] In addition, the commenter estimated the total cost to raise $99,000 of capital under the proposed rules to be $9,300 to $24,500 (9.4% to 24.7%); to raise $499,000 of capital to be $33,240 to $84,750 (6.7% to 17%); and to raise $1 million of capital to be $72,800 to $168,500 (7.3% to 16.9%). The commenter stated that the entry of new vendors into the market and ensuing competition may lead to a decline in some of these costs over time. Another commenter[1366] estimated that a $200,000 offering will incur the following average costs: legal fees of $10,000; intermediary fees of $20,000 (10%); accounting fees of $5,000; accounting review fees of $8,000; and other fees (transfer agent, campaign development, filing and other) of $7,000. A different commenter estimated that the cost to issuers could range from 26% to 601% of the offering amount over a five-year period, depending on the size of the offering, which does

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1361 *See* Proposing Release, Section III.B.3.

1362 *See*, *e.g.*, StartEngine Letter 2; FundHub Letter 2; Heritage Letter; SeedInvest Letter 1; SeedInvest Letter 2; Traklight Letter.

1363 *See* StartEngine Letter 2.

1364 The commenter does not specify whether these fees are expressed as a percentage of the amount sought or raised in the offering.

1365 We do not consider the costs associated with the incorporation or formation of the business itself to be part of the incremental costs of Regulation Crowdfunding, as these are costs associated with forming any business endeavor that relies on outside sources of capital.

1366 *See* Grassi Letter.

not account for additional estimated opportunity costs of internal personnel time of $35,000 to $85,000 over a five-year period.[1367] Some commenters referred to estimates of total costs without estimating individual components of those costs.[1368] Other commenters provided additional analysis of costs under different scenarios and offering sizes based on the estimates in the Proposing Release.[1369]

In general, commenters identified the following as the main costs for issuers in securities-based crowdfunding offerings: the intermediary fees; the costs of preparing, ensuring compliance with, and filing of Form C and Form C-AR; and the cost of accounting review or audit of financial statements.[1370] Below we discuss the comments received on each of these costs and any revisions to our estimates made in response.

With regard to intermediary fees, the estimates of the commenters that quantified these fees[1371] were generally very close to our estimates in the Proposing Release (5% to 15%). We

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1367 *See* SeedInvest Letter 1.

1368 *See, e.g.*, WealthForge Letter (suggesting that the costs associated with completing a crowdfunding transaction under the current regulations can be as high as one hundred thousand dollars, including audit fees, intermediary fees, legal fees and other offering costs); Berlingeri Letter (suggesting that the total cost would amount to between 15% and 20% of the offering); Traklight Letter (suggesting that the total cost would amount to between 15% and 20% of the offering for offerings above $100,000); FundHub Letter 1 (referring to potential costs, based on the Commission's estimates and the commenter's assumptions, of between $15,000 and $25,000 associated with raising $100,000); Harrison Letter and Ramsey Letter (referencing a Forbes estimate that the costs of disclosure documents, engaging an intermediary, performing background checks, and filing annual reports with the Commission might be upwards of $100,000). *See also SEC Proposes Crowdfunding Rules*, FORBES, Oct. 23, 2013, http://www.forbes.com/sites/deborahljacobs/2013/10/23/sec-proposes-crowdfunding-rules/.

1369 *See, e.g.*, EarlyShares Letter; RocketHub Letter; SeedInvest Letter 1.

1370 *But see* Growthfountain Letter (suggesting that crowdfunding issuers will also incur investor relations costs). We do not consider investor relations costs to be incremental to Regulation Crowdfunding, as these costs may be incurred by any business that relies on outside sources of capital and a widely dispersed investor base. However, to the extent that investment limitations in crowdfunding offerings increase the number of investors in a typical offering and to the extent that some investor relations costs are variable, issuers in crowdfunding offerings may incur higher investor relations costs than issuers in types of offerings that typically have fewer investors.

1371 *See* StartEngine Letter 2 (estimating portal fees of 6-15%). *See also* Grassi Letter (estimating an intermediary fee of $20,000 for a $200,000 offering, which amounts to 10% of the offering). *But see*

agree with the commenter that suggested that there is likely to be a fixed component to these costs that reflects a certain necessary level of due diligence and background screening, which will result in these costs as a percentage of offering size being higher for smaller offerings.[1372] Thus, we have revised our intermediary fee estimates in the following way: we project (as a percentage of offering proceeds) 5% to 15% for offerings of $100,000 or less, 5% to 10% for offerings between $100,000 and $500,000, and 5% to 7.5% for offerings above $500,000. Data on Regulation D offerings that involve intermediaries suggests that offerings of up to $1 million have an intermediary fee (commission and/or finder fee) of approximately 6.5% on average, which is within the range we estimate for larger crowdfunding offerings. Although crowdfunding intermediaries are not expected to provide issuers with services commensurate with those provided by underwriters in registered offerings (and, in fact, funding portals would be prohibited from doing so), the fees charged in a crowdfunding offering can be significantly larger on a percentage basis relative to the underwriting fees for registered offerings, which range from as high as 7% for initial public offerings to less than 1% for certain bond issuances.[1373] In general, to the extent that a significant component of these fees is fixed, the transaction costs for issuers will make smaller offerings more expensive on a percentage basis. As previously discussed, we

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Wefunder Letter (noting that, in contrast to the assumption in the Proposing Release, "good startups will pay a maximum of $0" and citing three accredited investor crowdfunding platforms that use a "carried interest" model for Rule 506 offerings, including the example of the commenter itself that does not charge a fee to startups but that charges investors a $25 fee and 10% carried interest (share of profits upon acquisition or initial public offering)).

1372 *See* Heritage Letter.

1373 *See, e.g.*, Hsuan-Chi Chen and Jay R. Ritter, *The Seven Percent Solution*, 55 J. FIN. 1105−1131 (2000); Mark Abrahamson, Tim Jenkinson, and Howard Jones, *Why Don't U.S. Issuers Demand European Fees for IPOs*? 66 J. FIN. 2055–2082 (2011); Shane A. Corwin, *The Determinants of Underpricing for Seasoned Equity Offers*, 58 J. FIN. 2249−2279 (2003); Lily Hua Fang, *Investment Bank Reputation and the Price and Quality of Underwriting Services*, 60 J. FIN. 2729−2761 (2005); Rongbing Huang and Donghang Zhang, *Managing Underwriters and the Marketing of Seasoned Equity Offerings*, 46 J. FIN. QUANT. ANALYSIS 141–170 (2011); Stephen J. Brown, Bruce D. Grundy, Craig M. Lewis and Patrick Verwijmeren, *Convertibles and Hedge Funds as Distributors of Equity Exposure*, 25 REV. FIN. STUD. 3077−3112 (2012).

believe that competition among crowdfunding venues and the potential development of new products and services may have a significant impact on these estimates over time.

The next major cost driver for issuers in securities-based crowdfunding offerings, as suggested by commenters, is the cost of preparing and filing disclosure documents and the internal burden of ensuring compliance with the disclosure requirements of the final rules. Issuers will incur costs to comply with the disclosure requirements and file the information in the new Form C: Offering Statement and Form C-U: Progress Update before the offering is funded. Thus, issuers will incur those costs regardless of whether their offerings are successful. In addition, for successful offerings, issuers will incur costs to comply with the ongoing reporting requirements and file information in the new Form C-AR: Annual Report.[1374]

Several commenters provided estimates of these costs. One commenter stated that Form C could be prepared by third-party service providers, such as itself, at much lower costs than those estimated by the Commission, noting that it can prepare Form C and other required disclosure documents, perform "bad actor" checks, verify investor status and fulfill other compliance requirements for an estimated total cost of $2,500 for an offering of $100,000 and that, in most cases, its services and associated legal fees will cost an issuer between $2,500 and $5,000 for an offering up to $500,000 and between $5,000 and $10,000 for an offering between $500,000 and $1,000,000.[1375]

Other commenters indicated that the compliance costs for issuers are likely to be higher than the Commission's estimates. One commenter indicated that the burden of completing Form C would likely exceed the 60 burden hours estimated by the Commission in the proposed rules

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[1374] *See* Rule 203(b) of Regulation Crowdfunding. *See also* Section II.B.3 above.

[1375] *See* FundHub Letter 2.

and that the sum of attorney and accounting fees and management and administrative time and other costs to prepare these required disclosures will likely exceed $10,500, except in cases of start-ups with no operating history.[1376] The commenter also noted that most Regulation D offerings, which tend to be less complex than crowdfunding offerings, based on the requirements in the proposed rules, incur accounting and legal fees above $2,500.[1377] Another commenter noted that issuers and intermediaries will likely incur higher attorney and accounting fees and financial and administrative burdens than estimated in the proposed rules but did not provide estimates.[1378]

One commenter submitted several estimates of the compliance costs associated with the final rules' disclosure requirements. In one comment letter, the commenter estimated the upfront compliance costs of the proposed rules to be potentially hundreds of hours in internal company time and $20,000 to $50,000 in outside professional costs and noted that such costs will likely be a significant deterrent to crowdfunding.[1379] In a different comment letter,[1380] this commenter stated that, based on an informal survey of potential vendors, it believes the costs of preparing a Form C-AR would range from $6,000 to $20,000, with the median being roughly $10,000. The commenter[1381] further estimated that an additional $15,000 worth of internal burden per year would be required to prepare Form C-AR and an additional $5,000 to $10,000 worth of internal

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1376 *See* Heritage Letter.

1377 *Id.*

1378 *See* NSBA Letter.

1379 *See* SeedInvest Letter 2.

1380 *See* SeedInvest Letter 1.

1381 *Id*.

burden would be required to prepare financial statements. In yet another comment letter,[1382] this commenter estimated the cost of ongoing disclosure obligations and ongoing requirements to file financial statements under the proposed rules to be upwards of $10,000 to $40,000 per year.

Based on these comments, we have revised our estimates of the compliance costs associated with the disclosure requirements of the final rules and Forms C and C-AR. On the lower end of the spectrum, one commenter suggested that the cost of preparing and filing these forms and the associated compliance costs would range from $3,000 to $9,000.[1383] Another commenter estimated preparation and compliance costs of $2,500 for an offering of $100,000, between $2,500 and $5,000 for an offering between $100,000 and $500,000, and between $5,000 and $10,000 for an offering between $500,000 and $1,000,000.[1384] We rely on this commenter's estimates of the costs of preparing and filling Form C for offerings of up to $100,000 and offerings between $100,000 and $500,000. Another commenter presented higher estimates, ranging from $6,000 to $20,000, with a median cost of $10,000, but did not provide estimates for different offering sizes.[1385] Given commenters' estimates, we think that the $6,000 to $20,000 estimate is more appropriate for larger offerings (of more than $500,000). Thus, to estimate the costs of preparing, filing, and complying with Form C for large offerings, we combine the cost ranges provided by the two commenters for these types of offerings, resulting in a cost estimate between $5,000 and $20,000. As in the Proposing Release, we estimate that the cost of preparing and complying with the requirements related to Form C-AR will be approximately two-thirds of that for Form C. We base this estimate on the fact that no offering-specific information will be

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1382 *See* SeedInvest Letter 4.

1383 *See* StartEngine Letter 2.

1384 *See* FundHub Letter 2.

1385 *See* SeedInvest Letter 1.

required in Form C-AR and issuers may thus be able to update disclosure previously provided on Form C. Our estimates of the costs of Forms C and C-AR are exclusive of the costs of an accounting review or audit, which are discussed separately below.

We expect that the cost of preparing and filing Forms C and C-AR will vary based on the characteristics of issuers, but we do not have the information to quantify such variation. For example, issuers with little operating activity may have less to disclose than issuers with more complex operations. Further, some issuers may rely to a greater extent on the services of outside professionals in preparing the required filings,[1386] while other issuers may choose to prepare and file the required forms without seeking the assistance of outside professionals.[1387] We also recognize the possibility that many if not all of the filing requirements may ultimately be performed by funding portals on behalf of issuers using their platforms.

The other significant cost for crowdfunding issuers, as identified by commenters, is the cost of an independent accounting review or audit. As discussed above, reviewed financial statements will be required in offerings of more than $100,000 but not more than $500,000, unless the issuer has audited statements otherwise available. Audited financial statements are required in offerings of more than $500,000.

In a change from the proposal, issuers that have not previously sold securities in reliance on Section 4(a)(6) will be permitted to provide reviewed financial statements in offerings of more than $500,000 but not more than $1,000,000, unless the issuer has audited statements otherwise available. This change is expected to greatly reduce the initial costs associated with providing

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1386 *See*, *e.g.*, McGladrey Letter (suggesting that issuers that are startups may rely on outside professional services to a greater extent, which would increase costs).

1387 For purposes of the PRA, we estimate that, for the average issuer, 25 percent of the burden associated with preparing and filing Form C and Form C-AR will be carried by outside professionals. *See* Section IV.C.1.a below.

financial statements for first-time crowdfunding issuers offering more than $500,000 but not more than $1,000,000. According to one commenter, the difference in cost for reviewed versus audited financial statements could easily run into tens of thousands of dollars.[1388]

Some commenters argued that the cost of reviewed or audited financial statements of startup companies, which is the type of companies expected to use Regulation Crowdfunding, would be lower than our estimates because such companies would be less complex and because a competitive industry would develop to support the compliance and disclosure needs of securities-based crowdfunding issuers.[1389] Commenters provided estimates for the cost of an accounting review of financial statements that generally ranged from $1,500 – $10,000.[1390] One commenter suggested that the cost of an accounting review is approximately 60% of the cost of an audit.[1391] Consistent with this comment, we also use an alternative way to estimate the cost of an accounting review: indirectly, from the cost of an audit.

Commenters provided several estimates of the cost of an audit for securities-based crowdfunding issuers, most of which ranged from $2,500 to $10,000.[1392] Other commenters,

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1388 *See* FundHub Letter 1. The comment letter also cites the commenter's article, which notes that "while a review could be in the range of $1000 in some cases, a formal audit by a CPA typically starts at $5,000 and could be much more." *See* Kendall Almerico, *Has The SEC Made Equity Crowdfunding Economically Unfeasible?* CROWDFUND INSIDER (Nov. 21, 2014), *available* at http://www.crowdfundinsider.com /2013/11/26291-sec-made-equity-crowdfunding-economicallyunfeasible.

1389 *See, e.g.*, CrowdFunding Network Letter; dbb*mckennon* Letter; Denlinger Letter 2; FundHub Letter 2; Holm Letter; StartEngine Letter 1; StartEngine Letter 2.

1390 *See, e.g.*, Grassi Letter (estimating the cost of accounting review for a $200,000 offering as $8,000); NPCM Letter (suggesting that the minimum cost to obtain an audit, or even a review, would be $5,000); StartEngine Letter 1 (estimating accounting review and audit costs of $1,500 – $10,000 for smaller, newer companies); StartEngine Letter 2 (estimating accounting review costs of $1,950 – $9,000).

1391 *See* Traklight Letter.

1392 *See, e.g.*, dbb*mckennon* Letter (estimating audit costs of $4,000 – $9,000 for new companies with limited historical operations); Denlinger Letter 2 (noting that audit costs may be in the range of $2,000 – $4,000 for a pre-revenue startup); FundHub Letter 2 (noting the emergence of CPA firms willing to perform a complete audit for a startup for $2,500 or less); NPCM Letter (suggesting that the minimum cost to obtain an audit, or even a review, would be $5,000); StartEngine Letter 1 (estimating accounting review and audit costs of

however, provided higher annual audit cost estimates of up to $20,000 – $30,000.[1393] Based on a compilation of audit fee data from reporting companies for fiscal year 2014, the average cost of an audit for an issuer with less than $1 million in market capitalization and less than $1 million in revenues is approximately $20,000.[1394] We estimate the audit cost to be approximately $2,500 to $30,000. In the Proposing Release, we estimated the audit cost to be $28,700, which falls within this range. Assuming that, as suggested by one commenter,[1395] the accounting review cost is approximately 60% of the audit cost, this range of audit costs yields an estimate of the accounting review cost of approximately $1,500 to $18,000. In the Proposing Release, we estimated the accounting review cost to be $14,350, which falls within this range. Estimates of the cost of an accounting review that we received from commenters also fall within this range. In light of the wide range of estimates provided by commenters for the cost of a review or audit of financial statements, we use in this release a range of estimates ($1,500 – $18,000 for the accounting review cost and $2,500 – $30,000 for the audit cost) instead of a single point estimate for these anticipated costs for offerings.

$1,500 – $10,000 for smaller, newer companies); StartEngine Letter 2 (estimating audit costs of $3,100 – $9,000).

1393 *See, e.g.,* Frutkin Letter (suggesting a "rough estimate of $30,000 per audit"); Graves Letter (suggesting that audit costs can be upwards of $18,000 to $25,000); Startup Valley Letter (suggesting that audit fees can be up to $10,000 for small startups with no financials and can exceed $20,000 for companies that have been in business for a few years); Traklight Letter (suggesting that audit costs can be up to $20,000).

1394 *See Audit Analytics, Auditor-Fees, available at* http://www.auditanalytics.com/0002/audit-data-company.php. The auditor fee database contains fee data disclosed by Exchange Act reporting companies in electronic filings since January 1, 2001. For purposes of our calculation, we averaged the auditor fee data for companies with both market capitalization and revenues of greater than zero and less than $1 million (the smallest subgroup of companies for which data is compiled). We note that the cost of an audit for many issuers conducting a securities-based crowdfunding offering in reliance on Section 4(a)(6) is likely to be lower than for the subset of Exchange Act reporting companies referenced above, because they likely would be at an earlier stage of development than issuers that file Exchange Act reports with us and, thus, could be less complex to audit.

1395 *See* Traklight Letter.

As discussed below, in a change from the proposal, the final rules do not require issuers to provide reviewed or audited financial statements in the annual report, unless such statements are otherwise available, which is expected to yield cost savings on an annual basis compared with the proposal.

The table below presents the main adjusted cost estimates for the final rules.[1396]

	Offerings of $100,000 or less	Offerings of more than $100,000, but not more than $500,000	Offerings of more than $500,000
Fees paid to the intermediary[1397]	$2,500 – $7,500	$15,000 – $30,000	$37,500 – $56,250
Costs per issuer for preparation and filing of Form C for each offering and related compliance costs	$2,500	$2,500 – $5,000	$5,000 – $20,000
Costs per issuer for preparation and filing of annual report on Form C-AR[1398] and related compliance costs	$1,667	$1,667 – $3,333	$3,333 – $13,333

1396 In addition to the compliance costs outlined in the table, issuers also will incur costs to (1) obtain EDGAR access codes on Form ID; (2) prepare and file progress updates on Form C-U; and (3) prepare and file Form C-TR to terminate ongoing reporting. These additional compliance costs are discussed further below. In addition, for purposes of the Paperwork Reduction Act ("PRA"), we provide burden estimates for each of these filings obligations in Section IV.C.1, below.

1397 For purposes of the table, we estimate the range of fees that an issuer would pay the intermediary assuming the following: (1) the fees would be calculated as a percentage of the offering amount ranging from 5% to 15% of the total offering amount for offerings of $100,000 or less, 5% to 10% for offerings between $100,000 and $500,000, and 5% to 7.5% for offerings of more than $500,000; and (2) the issuer is offering $50,000, $300,000 and $750,000, which are the mid-points of the offering amounts under each of the respective columns. The fees paid to the intermediary may, or may not, cover services to an issuer in connection with the preparation and filing of the forms identified in this table.

1398 As noted above, we estimate that these costs are approximately two-thirds of the costs for preparation and filing of Form C.

Costs per issuer for review or audit of financial statements	Not required	$1,500 – $18,000	$2,500 – $30,000 ($1,500 – $18,000 for first-time issuers raising more than $500,000 but not more than $1,000,000[1399])

We do not have additional data on the costs likely to be incurred by crowdfunding issuers to prepare the required disclosures beyond the information discussed above. Overall, we recognize that cost estimates may vary from issuer to issuer and from service provider to service provider. However, even with the additional accommodations provided in the final rules, the costs of compliance may be significant for some issuers.

b. General Disclosure Requirements

The statute and the final rules related to issuer disclosures are intended to reduce the information asymmetries that currently exist between small businesses and investors. Small private businesses typically do not disclose information as frequently or as extensively as public companies, if at all. Moreover, unlike public companies, small private businesses generally are not required to hire an independent accountant to review financial statements. When information about a company is difficult to obtain or the quality of the information is uncertain, investors are at risk of making poorly-informed investment decisions about that company.

Such information asymmetries may be especially acute in the securities-based crowdfunding market because the market includes startups and small businesses that have significant risk factors and other characteristics that may have led them to be rejected by other potential funding sources, including banks, VCs and angel investors. In addition, the securities-

[1399] First-time crowdfunding issuers within this offering range will be permitted to provide reviewed financial statements.

based crowdfunding market may attract unsophisticated investors who may not have the resources necessary to gather and analyze information about issuers before investing or to effectively monitor issuers after investing. Moreover, investment limits in securities-based crowdfunding offerings in reliance on Section 4(a)(6) will likely lead to investors having smaller stakes in the firm, which may reduce their incentives to monitor or gather information for a given investor. These considerations may give rise to adverse selection and moral hazard in offerings in reliance on Section 4(a)(6). For instance, some issuers may use capital to fund riskier projects than what was disclosed to investors, or they may not pursue their stated business objectives. If investors in securities-based crowdfunding have limited information about issuers or a limited ability to monitor such issuers, they may seek higher returns for their investment or choose to withdraw from the securities-based crowdfunding market altogether, which would increase the cost of capital to issuers and limit the capital formation benefits of the final rules. In addition, investors in offerings made in reliance on Section 4(a)(6) may make relatively small investments, due in part to the application of investment limitations. This potential dispersed investor base may make it difficult for investors to solve collective action problems in monitoring the issuer.

The statute and the final rules seek to reduce information asymmetries by requiring issuers to file specified disclosures with the Commission for offerings made in reliance on Section 4(a)(6) during the offering and on an annual basis thereafter.[1400] Issuers also are required to provide these disclosures to investors and, in the case of offering documents, to investors and the relevant intermediary. The disclosure requirements, which are described above,[1401] are more extensive than those required under some other existing exemptions from registration. For example,

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[1400] *See* Section 4A(b). *See also* Rules 201, 202 and 203 of Regulation Crowdfunding.

[1401] *See* Section II.B.1 above.

although the current requirements of Tier 1 Regulation A offerings include similar initial financial disclosures, issuers in Tier 1 offerings are not required to file ongoing reports.[1402] Issuers using the Rule 504 exemption under Regulation D to raise up to $1 million are not required to provide audited financial statements, and there are no periodic disclosure requirements. Regulation D offerings under Rules 505 and 506 for up to $2 million require issuers to provide audited current balance sheets (and unaudited statements of income, cash flows and changes in stockholders' equity) to non-accredited investors, but there are no periodic reporting requirements. The disclosure requirements in Regulation Crowdfunding are expected to benefit investors by enabling them to better evaluate the issuer and the offering, monitor how the issuer is performing over time and be aware of when the issuer may terminate its ongoing reporting obligations. This will allow investors with various risk preferences to invest in the offerings best suited for their risk tolerance, thus improving allocative efficiency.

The disclosure requirements also may improve informational efficiency in the market. Specifically, the required disclosure may provide investors with a useful benchmark to evaluate the issuer and compare the issuer to other private issuers both within and outside of the securities-based crowdfunding market.[1403] Additionally, disclosure by issuers engaging in crowdfunding transactions in reliance on Section 4(a)(6) may inform financial markets more generally about

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1402 However, issuers in Tier 1 Regulation A offerings are required to provide information about sales in such offerings and to update certain issuer information by electronically filing a Form 1-Z exit report with the Commission not later than 30 calendar days after the termination or completion of an offering. Further, Tier 1 offerings must be qualified by the Commission and are subject to state registration requirements. Issuers in Tier 2 offerings are subject to annual, semiannual and current reporting requirements. *See Regulation A Adopting Release*.

1403 *See* Christian Leuz and Peter Wysocki, *Economic Consequences of Financial Reporting and Disclosure Regulation: A Review and Suggestions for Future Research*, (Working Paper, University of Chicago) (2008), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1105398.

new consumer trends and new products, thus creating externalities that benefit other types of investors and issuers.

We recognize, however, that the disclosure requirements also will have associated limitations and costs, including the direct costs of preparation, certification, independent accounting review (when necessary) and dissemination of the disclosure documents. As noted above, the disclosure requirements for offerings made in reliance on Section 4(a)(6) are more extensive, in terms of breadth and frequency, than those for other exempt offerings. The statute also provides us with the discretion to impose additional requirements on issuers engaging in crowdfunding transactions, and in some cases, the final rules require issuers to disclose information beyond what is specifically mandated by the statute.[1404] We recognize that these additional discretionary disclosure provisions may impose additional compliance costs on issuers compared with the proposal. However, we believe these provisions will improve investor decision-making and may ultimately benefit issuers by improving price efficiency in the securities-based crowdfunding market. Although requiring less disclosure could impose lower compliance costs, we believe that the disclosure requirements we are adopting appropriately consider the need to enhance the ability of issuers relying on Section 4(a)(6) to raise capital while enabling investors to make informed investment decisions. In response to the suggestion by some commenters that issuers not be required to disclose information in multiple places,[1405] under the final rules, an issuer is not required to repeat disclosure that is already provided in the issuer's financial statements. This may help to mitigate the cost of compliance for issuers.

1404 *See* Section 4A(b)(5). *See also* Section II.B.1.a.i(g) for a description of the additional disclosure requirements.

1405 *See, e.g.*, EY Letter (noting that certain required disclosure would be included in an issuer's financial statements); Grassi Letter (same).

We note that the disclosure requirements may have indirect costs to the extent that information disclosed by issuers relying on Section 4(a)(6) can be used by their competitors, resulting in a potential loss of a competitive advantage or intellectual property, particularly for high-growth issuers and issuers engaged in significant research and development. Requiring significant levels of disclosure at an early stage of an issuer's lifecycle may affect an issuer's competitive position and may limit the use of the exemption in Section 4(a)(6) by issuers who are especially concerned with confidentiality. These disclosure costs also may make other types of private offerings more attractive to potential securities-based crowdfunding issuers. For example, the 2013 changes to Rule 506 of Regulation D,[1406] which allow for general solicitation, subject to certain conditions, may make it a more attractive option for small business financing and, thus, may divert potential issuers from crowdfunding.

In addition, under the statute and the final rules, issuers that complete a crowdfunding offering in reliance on Section 4(a)(6) are subject to ongoing reporting requirements,[1407] which will increase compliance costs. The ongoing reporting, however, may provide a liquidity benefit for secondary sales of securities issued in crowdfunding transactions and make the prices of such securities more informationally efficient, should a secondary market develop.

c. Financial Condition and Financial Statement Disclosure Requirements

Consistent with the statute, the final rules require narrative disclosure about the issuer's financial condition, including, to the extent material, liquidity, capital resources and the issuer's historical results of operations.[1408] We expect that this discussion will inform investors about the

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1406 *See Rule 506(c) Adopting Release*, note 5.

1407 *See* Rule 202 of Regulation Crowdfunding.

1408 *See* Rule 201(s) of Regulation Crowdfunding. *See also* Section II.B.1.a.(ii)(a) above.

financial condition of the issuer, without imposing significant costs on issuers, because issuers likely will already have such information readily available. In addition, the final rules do not prescribe the content or format for this information.

With respect to the requirement to provide financial statements, the final rules implement tiered financial disclosure requirements based on the aggregate amount of securities offered and sold in reliance on Section 4(a)(6) during the preceding 12-month period, inclusive of the offering amount in the offering for which disclosure is being provided.[1409] The disclosure requirements will provide investors with more information than might otherwise be obtained in private offerings, but also may create additional costs for those issuers that have limited financial and accounting expertise necessary to produce the financial disclosures envisioned by the statute and the final rules.

The final rules, consistent with the proposed rules, require issuers to provide a complete set of their financial statements (balance sheets, statements of comprehensive income, statements of cash flows and statement of changes in stockholders' equity) that are prepared in accordance with U.S. GAAP and cover the shorter of the two most recently completed fiscal years or the period since inception.[1410] We could have chosen an alternative that allows financial statements to be prepared in accordance with other comprehensive bases of accounting, as some commenters suggested.[1411] Such an alternative may have mitigated costs for some issuers, especially those

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1409 *See* Rule 201(t) of Regulation Crowdfunding. *See also* Section II.B.1.a.(ii)(b) above.

1410 *See* Instruction 3 to paragraph (t) of Rule 201 of Regulation Crowdfunding.

1411 *See, e.g.*, ABA Letter (for offerings of $100,000 or less, but stating that the Commission could require providing U.S. GAAP financial statements if available); AICPA Letter; CFIRA Letter 5; CFIRA Letter 7; CrowdCheck Letter 4; EarlyShares Letter; EY Letter (for offerings of $100,000 or less, unless U.S. GAAP financial statements are available); Grassi Letter; Graves Letter (for issuers with less than $5 million in revenue); Mahurin Letter (stating that simple Excel spreadsheets accompanied by bank records should meet the financial statement requirements); Milken Institute Letter (for early-stage issuers); NFIB Letter; SBEC

smaller issuers that historically have prepared their financial statements in accordance with other comprehensive bases of accounting rather than U.S. GAAP. However, as we discussed above, this alternative would reduce the comparability of financial statements across issuers and might not provide investors with a fair representation of a company's financial position and results of operations. Further, it may be difficult for investors to determine whether the issuer complied with such basis of accounting.[1412]

The final rules also specify that an issuer may conduct an offering in reliance on Section 4(a)(6) using financial statements for the fiscal year prior to the most recently completed fiscal year, provided that not more than 120 days have passed since the end of the issuer's most recently completed fiscal year, and financial statements for the most recently completed fiscal year are not otherwise available.[1413] This may impose a cost on investors to the extent that the investors do not have more current financial information about the issuer. However, this concern is somewhat mitigated by the requirement that issuers include a discussion of any material changes or trends known to management in the financial condition and results of operations subsequent to the period for which financial statements are provided.[1414]

Requiring financial statements covering the two most recently completed fiscal years is expected to benefit investors by providing a basis for comparison against the most recently completed fiscal year and by allowing investors to identify changes in the development of the business. Compared to an alternative that we could have selected, that of requiring financial

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Letter; StartupValley Letter; Tiny Cat Letter (for offerings of less than $500,000); Whitaker Chalk Letter (for offerings of less than $500,000 if the issuer has an asset or income level below a certain level).

1412 *See* Section II.B.1.a.(ii)(b) above.

1413 *See* Instruction 10 to paragraph (t) of Rule 201 of Regulation Crowdfunding.

1414 *See* Rule 201(s) of Regulation Crowdfunding.

statements covering only the most recently completed fiscal year, as some commenters suggested,[1415] requiring a second year of financial statements will to some degree increase the cost for the issuer. Also, to the extent that the issuer had little or no operations in the prior year, the benefit of comparability may not be realized. We recognize that many crowdfunding issuers may not have any financial history, and investors may make investment decisions without a track record of issuer performance, relying largely on the belief that an issuer can succeed based on their business plan and other factors. Nevertheless, for those issuers that do have a financial history, we believe this disclosure can contribute to better informed investment decisions and improve the overall allocative efficiency of the securities-based crowdfunding market.

For offerings of $100,000 or less, the final rules require the issuer to provide financial statements that are certified by the principal executive officer to be true and complete in all material respects.[1416] The final rules include a form of certification for the principal executive officer to provide in the issuer's offering statement, which we believe will help issuers comply with the certification required by the statute and the final rules.[1417] However, if reviewed financial statements or audited financial statements are otherwise available, they must be provided.[1418]

The proposed rules would have required income tax returns for the most recently completed year (if any). In a change from the proposed rules, consistent with the suggestions of some commenters and to respond to privacy concerns,[1419] the final rules do not require complete

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1415 *See, e.g.*, Denlinger Letter 1; EY Letter; Fryer Letter; Grassi Letter; Joinvestor Letter; Public Startup Letter 2; RFPIA Letter; RocketHub Letter.

1416 *See* Section 4A(b)(1)(D)(i). *See also* Rule 201(t)(1) of Regulation Crowdfunding.

1417 *See* Instruction 4 to paragraph (t) of Rule 201 of Regulation Crowdfunding.

1418 *See* Rule 201(t)(1) of Regulation Crowdfunding.

1419 *See, e.g.*, AICPA Letter (stating that disclosure of an issuer's tax return "…has the potential to cause serious problems. Tax returns are intended to be confidential and should remain so."); Public Startup Letter 2;

tax returns and instead require that an issuer disclose its total income, taxable income and total tax, or the equivalent line items from the applicable form, and have the principal executive officer certify that those amounts reflect accurately the information in the issuer's federal income tax returns.[1420] We believe that the requirement to provide selected items from the return, rather than the return itself, will alleviate some of the privacy concerns for issuers. This change may increase record keeping costs for issuers and give rise to potential transcription errors. It also may reduce the amount of information available to investors, but as we noted in the Proposing Release, it is not clear to what extent all of the information presented in a tax return would be useful for an investor evaluating whether or not to purchase securities from the issuer. Finally, although principal executive officers will incur some incremental liability for their certification that these amounts reflect accurately the information in the issuer's federal income tax return, we do not expect this change from the proposal to impose substantial additional costs on officers or issuers given the limited scope of the required certification.

Moreover, the final rules specify that if an issuer is offering securities in reliance on Section 4(a)(6) before filing a tax return for the most recently completed fiscal year, the issuer may use information from the tax return filed for the prior year, on the condition that the issuer provides information from the tax return for the most recently completed fiscal year when it is filed, if it is filed during the offering period.[1421] This accommodation is expected to benefit issuers by enabling them to engage in transactions during the time period between the end of their

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RocketHub Letter; SBM Letter; Wilson Letter (suggesting that personal income tax information should be on a voluntary basis only); Zhang Letter.

1420 *See* Rule 201(t)(1) of Regulation Crowdfunding.

1421 *See* Instruction 6 to paragraph (t) of Rule 201 of Regulation Crowdfunding.

fiscal year and when they file their tax return for that year. This may impose a cost on investors because they might not receive the most up-to-date tax information about the issuer.

The proposed rules would have required financial statements for offerings exceeding $100,000 but not exceeding $500,000 to be reviewed by a public accountant independent of the issuer and financial statements for offerings exceeding $500,000 to be audited by a public accountant independent of the issuer. The final rules specify that the required financial statements must be reviewed by a public accountant that is independent of the issuer for offerings exceeding $100,000 but not exceeding $500,000.[1422] If, however, financial statements of the issuer are available that have been audited by a public accountant that is independent of the issuer, the issuer must provide those financial statements instead and need not include the reviewed financial statements.[1423]

Similar to the proposal, issuers in offerings exceeding $500,000 must provide audited financial statements. In a change from the proposal, the final rules specify that issuers that have not previously sold securities in reliance on Section 4(a)(6) and are conducting offerings with a target offering amount exceeding $500,000 but not exceeding $1,000,000 can provide reviewed financial statements, unless audited financial statements are otherwise available.[1424] Audited financial statements can benefit investors in evaluating offerings by issuers with substantive prior business activity by providing them with potentially higher-quality financial statements. However, as noted by a number of commenters[1425] and discussed above, requiring audited

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1422 *See* Rule 201(t)(2) of Regulation Crowdfunding.

1423 *Id*.

1424 *See* Rule 201(t)(3) of Regulation Crowdfunding. *See also* Section II.B.1.a.ii.

1425 *See, e.g.*, AEO Letter; Angel Letter 1; AWBC Letter; CFIRA Letter 5; CfPA Letter; CrowdFundConnect Letter; EarlyShares Letter; EMKF Letter; EY Letter; Finkelstein Letter; FundHub Letter 1; Generation Enterprise Letter; Grassi Letter; Graves Letter; Guzik Letter 1; Hakanson Letter; Holland Letter; Johnston

financial statements could significantly increase the cost to issuers compared to requiring reviewed financial statements.[1426] Further, for issuers that are newly formed, with no or very limited operations, and for small issuers, the benefit of the audit may not justify its cost.

As discussed above,[1427] the approach in the final rules of requiring reviewed financial statements rather than audited financial statements, unless otherwise available, for first-time crowdfunding issuers that undertake offerings of more than $500,000 but not more than $1,000,000 is expected to reduce the costs associated with financial statements for such first-time issuers compared to the proposed requirement of audited financial statements for all issuers in offerings of more than $500,000. This accommodation is expected to alleviate the significant upfront cost of an audit for first-time issuers that have not yet raised capital in a crowdfunding offering and may be more financially constrained. To the extent that their financing needs have not been met through alternative financing methods, first-time crowdfunding issuers are likely to be more financially constrained than issuers that have already established a track record of successful crowdfunding offerings. We recognize, however, that there are costs associated with this accommodation. Not requiring audited financial statements for offerings of more than $500,000 but not more than $1,000,000 by first-time issuers may reduce the quality of financial disclosure, which may be a more significant concern for new crowdfunding issuers due to the fact that their more limited track record may translate into a higher level of information asymmetry between issuers and investors. The potentially reduced quality of financial disclosure associated

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Letter; Kickstarter Coaching Letter; McGladrey Letter; Milken Institute Letter; NACVA Letter; NFIB Letter; NPCM Letter; NSBA Letter; PBA Letter; Reed Letter; RocketHub Letter; Saunders Letter; SBA Office of Advocacy Letter; SBEC Letter; SBM Letter; Seyfarth Letter; Verrill Dana Letter; WealthForge Letter; Wefunder Letter; Woods Letter; Zeman Letter.

1426 *See also* Section III.B.3.a.

1427 *Id*.

with offerings of more than $500,000 by first-time issuers may affect the likelihood of detecting fraud, which would decrease investor protection. To the extent that investors anticipate such increased risks, issuers may face a higher cost of capital or be unable to raise the entire amount offered, which would diminish the capital formation benefits of the final rule. We note that some first-time issuers in offerings of more than $500,000 but not more than $1,000,000may have audited statements otherwise available, which could partly mitigate the described effects. We also note that some first-time issuers concerned about investor confidence in the quality of their financial statements may voluntarily provide audited financial statements.

Tiered disclosure requirements aim to partially mitigate the impact of the fixed component of compliance costs on issuers in smaller securities-based crowdfunding offerings. However, it is possible that the thresholds may have an adverse competitive effect on some issuers. For example, the cost of reviewed financial statements may cause issuers in offerings exceeding but close to $100,000 to incur significantly higher offering costs as a percentage of the amount offered compared to issuers offering less than but close to $100,000. Similarly, the cost of audited financial statements may cause issuers in follow-on crowdfunding offerings exceeding but close to $500,000 to incur significantly higher offering costs as a percentage of the amount offered compared to issuers in offerings of less than but close to $500,000. We note, however, that the issuer has the ability to select its offering amount, and since the choice of offering amount determines which financial statement requirements will apply to its offering, the issuer, by choosing its offering amount, effectively also chooses its financial statement requirements.

We considered the alternative of exempting issuers with no operating history or issuers that have been in existence for fewer than 12 months from the requirement to provide financial statements. We believe that financial statements contain valuable information that can aid

investors in making better informed decisions, particularly, when evaluating early-stage issuers characterized by a high degree of information asymmetry. We also expect that other accommodations in the final rules will help alleviate some of these issuer compliance costs.

Similar to the proposed rules, financial statements must be reviewed in accordance with SSARS issued by the AICPA.[1428] Although we could have chosen to develop a new review standard for purposes of the final rules, we believe that issuers will benefit from using the AICPA's widely-utilized review standard. We believe that many accountants reviewing financial statements of issuers raising capital in reliance on Section 4(a)(6) are familiar with the AICPA's standards and procedures for review, which should help to partly mitigate review costs.

As described above, the final rules require certain financial statements to be reviewed or audited by a public accountant that is independent of the issuer.[1429] In a change from the proposed rules, the final rules permit the use of independence standards set forth in Rule 2-01 of Regulation S-X or the independence standards of the AICPA.[1430] This change to allow the use of AICPA standards may reduce issuer compliance costs to the extent that there are higher costs associated with engaging an accountant that satisfies the independence standards set forth in Rule 2-01 of Regulation S-X. The change also will increase the number of public accountants able to perform the reviews or audits, which may lead to a decrease in the price of their services and thus a decrease in the direct issuance costs to issuers compared with the proposal. The benefit from this change will accrue to issuers making offerings of $100,000 to $1,000,000. To the extent that the AICPA independence standards impose fewer restrictions with respect to potential conflicts of

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1428 *See* Rule 201(t)(2) of Regulation Crowdfunding. *See also* Instruction 8 to paragraph (t) of Rule 201 of Regulation Crowdfunding.

1429 *See* Section II.B.1 above.

1430 *See* Instruction 10 to paragraph (t) of Rule 201 of Regulation Crowdfunding.

interest than the independence standards in Rule 2-01 of Regulation S-X, however, this accommodation may weaken investor protection. Moreover, any decrease in investor confidence in the reliability of financial statements as a result of this change will limit the capital formation benefits of the final rules.

In addition, the final rules require an issuer to file a signed review report or audit report, whichever is applicable, and notify the public accountant of the issuer's intended use of the report in the offering.[1431] This can impose an additional cost on issuers to the extent that the accountant or auditor increases the fee associated with the review or audit to compensate for any additional liability that may result from the requirement to file the report. As discussed above,[1432] in a change from the proposal, the final rules do not permit qualified audit reports. This change may impose an additional cost on issuers, which we are not able to quantify. However, this change is expected to provide investors with more reliable financial statements, which should enable investors to better evaluate the prospects of issuers relying on Section 4(a)(6) and thus make better informed investment decisions. By providing investors with a greater degree of confidence in the reliability of the financial information, audited financial statements will reduce the information asymmetry about the issuer's financial condition that exists between issuers and potential investors. This decrease in information asymmetry may lead to greater capital formation.

In a change from the proposed rules, the final rules do not require financial statements in the annual report that meet a standard of review equal to the highest standard provided in a prior offering.[1433] The final rules require an annual report to include financial statements of the issuer

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1431 *See* Instructions 8 and 9 to paragraph (t) of Rule 201 of Regulation Crowdfunding.

1432 *See* Section II.B.1.a.(ii)(b) above.

1433 *See* Section II.B.2.c above.

to be certified by the principal executive officer of the issuer as true and complete in all material respects.[1434] Issuers that otherwise have available financial statements that have been reviewed or audited by an independent certified public accountant, must provide them and will not be required to have the principal executive officer certification.[1435] As discussed above, these changes will reduce the compliance costs to issuers compared with the proposal.[1436] At the same time, they may reduce the quality of the ongoing financial statements, resulting in a potential decrease in investor protection and investor confidence in the quality of these financial statements. We note that some issuers may have reviewed or audited financial statements otherwise available, which would partly mitigate this concern. In addition, an issuer is able to voluntarily provide financial statements that meet a higher standard, so if an issuer is concerned about investor confidence in the quality of financial statements, it can choose to provide reviewed or audited financial statements.

d. Issuer Filing Requirements

As discussed above, issuers will incur costs to prepare and file the various disclosures required under Regulation Crowdfunding.[1437] The statute requires issuers to file and provide to investors certain specified information at the time of offering, such as information about the issuer, officers and directors, and certain shareholders, a description of the business, a description of the purpose and intended use of proceeds, target offering amount and the deadline to reach it, offering price (or the method for determining the price) and other terms of the offering, a

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1434 *See* Rule 202(a) of Regulation Crowdfunding.

1435 *Id*.

1436 *See* Section III.B.3.a. above.

1437 *See* Section III.B.3.a. above.

description of the financial condition of the issuer, as well as certain other disclosures.[1438] These disclosure requirements are expected to strengthen investor protection and enable investors to make better informed investment decisions. The statute does not specify a format that issuers must use to present the required disclosures to the Commission. As noted above, the final rules require issuers to file the mandated disclosure on EDGAR using new Form C.[1439]

Form C requires certain disclosures to be submitted using an XML-based filing,[1440] while allowing the issuer to customize the presentation of other required disclosures. This approach provides issuers with the flexibility to present the required disclosures in a cost-effective manner, while also requiring the disclosure of certain key offering information in a standardized format, which we believe will benefit investors and help facilitate capital formation.

We expect that requiring certain disclosures to be submitted using XML-based filings will produce benefits for issuers, investors and the Commission. For instance, using information filed pursuant to these requirements, investors can track capital generated through crowdfunding offerings without manually inspecting each filing. The ability to efficiently collect information on all issuers also can provide an incentive for data aggregators or other market participants to offer services or analysis that investors can use to compare and choose among different offerings. For example, reporting key financial information using XML-based filings will allow investors, analysts and data aggregators to more easily compile, analyze and compare information about the capital structure and financial position of various issuers. XML-based filings also will provide the Commission with data about the use of the new crowdfunding exemption that will allow the

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1438 *See* Rule 201 of Regulation Crowdfunding. *See also* Section II.B.1 above.

1439 *See* Rule 203(a) of Regulation Crowdfunding. *See also* Section II.B.3 above.

1440 *See* Instruction to paragraph (a)(1) of Rule 203 of Regulation Crowdfunding. *See also* Section II.B.3 above.

Commission to evaluate whether the rules implementing the exemption include appropriate investor protections and are effectively facilitating capital formation.

Certain provisions of the filing requirements in the final rules provide flexibility and potentially reduce the compliance burden compared with the proposal. The final rules allow issuers to customize the presentation of their non-XML disclosures and file those disclosures as exhibits to Form C in PDF format as official filings, consistent with the suggestions of some commenters.[1441] In addition, the final rules include an optional Question and Answer ("Q&A") format that issuers may opt to use to provide the disclosures that are not required to be filed in XML format.[1442] Relative to some other possible formats, this Q&A format may facilitate the preparation of the Form C disclosures by crowdfunding issuers. To the extent that this provision lowers the compliance cost for issuers, it may encourage greater use of Regulation Crowdfunding for raising capital.

The final rules require that issuers file a Form C-U: Progress Update to describe the progress of the issuer in meeting the target offering amount.[1443] In a change from the proposed rules, based on concerns expressed by commenters, the final rules permit issuers to satisfy the progress update requirement by relying on the relevant intermediary to make publicly available on the intermediary's platform frequent updates about the issuer's progress toward meeting the target offering amount. This change is expected to mitigate some of the direct cost for the issuer without reducing the amount of contemporaneous information available to investors. However, an issuer relying on the intermediary to make publicly available frequent progress updates must still file a

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1441 *See, e.g.*, CFIRA Letter 6; CFIRA Letter 7; CrowdCheck Letter 1; Grassi Letter; Hackers/Founders Letter; RocketHub Letter; Wefunder Letter; Wilson Letter.

1442 *See* Item 1 of General Instruction III to Form C.

1443 *See* Rule 203(a)(3) of Regulation Crowdfunding. *See also* Sections II.B.1.b and II.B.3 above.

Form C-U at the end of the offering to disclose the total amount of securities sold in the offering.[1444] Although the final offering information likely will be available on the registered intermediary's website, having the information available on EDGAR will allow comparisons across platforms and provide ongoing access to historical information for future investor analyses that may otherwise be difficult or impossible to perform by accessing information from each individual portal. We expect the costs of preparing updates on Form C-U to vary among issuers but to be relatively small.[1445]

As noted above, the statute also requires an issuer to file and provide to investors information about the issuer's financial condition on at least an annual basis, as determined by the Commission.[1446] Ongoing disclosure requirements are expected to strengthen investor protection. Ongoing disclosure requirements are also expected to facilitate better informed investment decisions in secondary market transactions and enhance the informational efficiency of prices of crowdfunding securities, should a secondary market for such securities develop. To implement this statutory requirement, the final rules require any issuer that has sold securities in a crowdfunding transaction in reliance on Section 4(a)(6) to file annually with the Commission a new Form C-AR: Annual Report, no later than 120 days after the end of each fiscal year covered by the report.[1447] We believe that annual reports will inform investors in their portfolio decisions and can enhance price efficiency. Moreover, as discussed above, under the statute and the final

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1444 *See* Rule 203(a)(3)(iii) of Regulation Crowdfunding.

1445 For purposes of the PRA, we estimate that an issuer's compliance with the Form C-U requirement will result, on average, in approximately 0.50 burden hours per issuer. *See* Section IV.C.1.a below.

1446 *See* Section 4A(b)(4).

1447 *See* Rule 202(a) of Regulation Crowdfunding. *See also* Section II.B.2 above for a discussion of the disclosure requirements of Form C-AR.

rules, the securities will be freely tradable after one year,[1448] and therefore, this information also will benefit potential future holders of the issuer's securities by enabling them to update their assessments as new information is made available through the annual updates, potentially allowing for more efficient pricing. More generally, these continued disclosures also may help facilitate the transfer of securities in secondary markets after the one-year restricted period ends, which can mitigate some of the potential liquidity issues that are unique to the securities-based crowdfunding market, as discussed above.

As an alternative, we could have added a current reporting requirement, consistent with the view of some commenters that there may be major events that occur between annual reports about which investors would want to be updated.[1449] Such an alternative could result in better informed investment decisions. We are concerned, however, that the benefits of a current reporting requirement may not justify the additional compliance costs associated with such a requirement, especially given the size and early stage of development of the issuers likely to be involved in offerings in reliance on Section 4(a)(6).

Any issuer terminating its annual reporting obligations will be required to file a notice under cover of Form C-TR: Termination of Reporting to notify investors and the Commission that it will no longer file and provide annual reports pursuant to the requirements of Regulation Crowdfunding.[1450] The final rules enable issuers to terminate reporting if: (1) the issuer becomes a reporting company required to file reports under Exchange Act Sections 13(a) or 15(d); (2) the issuer or another party repurchases all of the securities issued pursuant to Securities Act

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1448 *See* Section 4A(e). *See also* Rule 501 of Regulation Crowdfunding.

1449 *See, e.g.*, ABA Letter; Angel Letter 1; Denlinger Letter 1; EY Letter; Grassi Letter; Hackers/Founders Letter; RocketHub Letter.

1450 *See* Rule 203(b)(3) of Regulation Crowdfunding.

Section 4(a)(6), including any payment in full of debt securities or any complete redemption of redeemable securities; or (3) the issuer liquidates or dissolves its business in accordance with state law.[1451] We expect the costs of preparing Form C-TR to vary among issuers but to be relatively small.[1452]

In a change from the proposed rules, after considering the comments, the final rules also permit termination of ongoing reporting in two additional circumstances: (1) the issuer has filed at least one annual report and has fewer than 300 holders of record, or (2) the issuer has filed annual reports for at least the three most recent years and has total assets not exceeding $10,000,000.[1453] This change is expected to mitigate some of the compliance cost for small issuers and make the final rules a more attractive option for capital formation among small issuers, and at the same time, help to ensure that larger issuers with a significant number of investors continue to provide relevant disclosure.

This change may, however, make relevant information about the financial condition of certain issuers no longer available to investors, resulting in less informed investor decisions. This change may affect a large number of securities-based crowdfunding offerings, since it is likely that many crowdfunding issuers will either have fewer than 300 holders of record or assets below $10 million. Termination of ongoing reporting may result in a decrease in investor protection, particularly in the presence of an investor base with a limited degree of sophistication. Allowing issuers to terminate ongoing reporting can make monitoring of the issuer more difficult for investors and can potentially make it more difficult to detect fraud. We note, however, that the

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1451 *See* Rule 202(b) of Regulation Crowdfunding.

1452 For the purposes of the PRA, we estimate that issuers will spend, on average, approximately 1.5 burden hours to complete this task. *See* Section IV.C.1.a below.

1453 *Id.*

investment limits in the final rules serve to limit the amount of each investor's capital that is exposed to these and other risks of securities-based crowdfunding offerings. We further note that the investment amounts involved in these transactions might limit a typical investor's incentives to analyze the information contained in ongoing disclosures and to monitor issuers, even if all issuers are required to provide ongoing disclosures.

Nevertheless, the risk that an issuer in a securities-based crowdfunding offering may terminate ongoing reporting in the future may discourage prospective investors from making an initial investment in offerings in reliance on Section 4(a)(6) or may cause issuers to obtain lower valuations for the securities they offer, which may limit some of the capital formation benefits of the final rules. We note that issuers who believe that increased investor confidence justifies the cost of annual reporting would be able to continue ongoing reporting voluntarily.

Termination of ongoing reporting may also reduce the informational efficiency of prices and secondary market liquidity, making it more difficult for investors to exit their holdings after the expiration of resale restrictions. A lack of ongoing reporting may reduce the likelihood that a secondary market for such securities develops. We recognize, however, that a secondary market for securities in offerings in reliance on Section 4(a)(6) may not develop even if all issuers are required to provide ongoing reports.

The asset size cap in one of the termination thresholds may create adverse competitive effects for issuers close to but above the termination threshold.

e. Advertising – Notice of Offering

The statute and the final rules prohibit an issuer from advertising the terms of the offering, except for notices that direct investors to an intermediary's platform.[1454] The terms of the offering include the amount offered, the nature of the securities, price of the securities and length of the offering period.[1455] The final rules allow an issuer to publish a notice about the terms of the offering made in reliance on Section 4(a)(6), subject to certain limitations on the content of the notice.[1456] The notices are similar to the "tombstone ads" permitted under Securities Act Rule 134,[1457] except that the final rules require the notices to direct investors to the intermediary's platform, through which the offering made in reliance on Section 4(a)(6) is being conducted.

We believe this approach will allow issuers to generate interest in offerings and to leverage the power of social media to attract investors, potentially resulting in enhanced capital formation. At the same time, we believe it also will protect investors by limiting the ability of issuers to provide certain advertising materials without also directing investors to the disclosures, available on the intermediary's platform, that are required for an offering made in reliance on Section 4(a)(6). Moreover, this requirement is not expected to impose costs on market participants.

As an alternative, we could have required communications about the offering to be conducted through the intermediary, as suggested by some commenters.[1458] To the extent that an issuer might be able to inform more investors about its offering if it is not limited to

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1454 *See* Section 4A(b)(2). *See also* Rule 204 of Regulation Crowdfunding.

1455 *See* Instruction to Rule 204 of Regulation Crowdfunding.

1456 *See* Rule 204(b) of Regulation Crowdfunding. *See also* Section II.B.4 above.

1457 17 CFR 230.134.

1458 *See* Hackers/Founders Letter (supporting the issuer being able to repost the communications elsewhere so long as it first appeared through the intermediary); Joinvestor Letter.

communications through the intermediary's platform, this alternative might limit the issuer's ability to inform a wide range of investors about its offering. Limited recognition among prospective investors might be a particularly significant hurdle for early-stage or small issuers. As another alternative, we could have required issuers to file advertising notices with the Commission and/or the relevant intermediary, as suggested by other commenters.[1459] While this could increase the likelihood of issuer compliance with advertising restrictions, it also would impose an additional cost on the issuer. Overall, in light of the restrictions on advertising already in place, it is not clear to what extent, if any, additional restrictions would enhance investor protection.

Some commenters, suggesting that advertising restrictions are unnecessary because sales must occur through an intermediary's platform,[1460] recommended allowing the issuer more leeway to publicize its business or offering on its own website or social media platform so long as the specific terms of the offering could be found only through the intermediary's platform,[1461] and recommended allowing advertising notices to have a section for supplemental information highlighting certain intangible purposes such as a particular social cause.[1462] The alternative of relaxing or eliminating restrictions on advertising could enhance capital formation efforts of issuers. However, it might also result in a cost to investors if they make less informed investment decisions based on incomplete or selectively presented information about the offering contained in advertising materials.

1459 *See, e.g.*, Commonwealth of Massachusetts Letter; CFIRA Letter 6.

1460 *See, e.g.*, FundHub Letter 1; Seed&Spark Letter (noting the proposed advertising restrictions will restrict the ability of filmmakers to market and raise money for their films); Arctic Island Letter 5; PeoplePowerFund Letter.

1461 *See* Fryer Letter.

1462 *See* RocketHub Letter.

f. Compensation of Persons Promoting the Offering

The statute and the final rules prohibit an issuer from compensating, or committing to compensate, directly or indirectly, any person to promote the issuer's offering through communication channels provided by the intermediary unless the issuer takes reasonable steps to ensure that such person clearly discloses the receipt of such compensation (both past and prospective) each time a promotional communication is made.[1463]

We believe this requirement will benefit the securities-based crowdfunding market by allowing investors to make better informed investment decisions. Although the requirement to take steps to ensure disclosure of compensation paid to persons promoting the offering will impose compliance costs on issuers, we believe that investors will benefit from knowing if the comments about the investment they are considering are being made by a promoter who is compensated by the issuer and therefore may not be providing an independent, disinterested perspective.

The final rules also require that an issuer not compensate or commit to compensate, directly or indirectly, any person to promote its offerings outside of the communication channels provided by the intermediary, unless the promotion is limited to notices that comply with the advertising rules.[1464] We believe this will similarly serve to improve investors' ability to make informed judgments about the information they encounter through various communication channels about the issuer, and thus, to make better informed investment decisions.

[1463] *See* Section 4A(b)(3). *See also* Rule 205 of Regulation Crowdfunding and Section II.B.5 above.

[1464] *See* Rule 205 of Regulation Crowdfunding. *See also* Section II.B.5 above.

g. Oversubscription and Offering Price

The final rules permit an issuer to accept investments in excess of the target offering amount, subject to the $1 million limitation, but require the issuer to disclose the maximum amount the issuer will accept and how shares in oversubscribed offerings will be allocated.[1465] We continue to believe that permitting oversubscriptions will provide flexibility to issuers so that they can raise the amount of capital they deem necessary to finance their businesses. Given the uncertainty on the part of the issuer about potential market demand for the issuer's securities, we believe it is valuable for issuers to have the option to permit oversubscriptions. For example, permitting oversubscriptions will allow an issuer to raise more funds, while lowering compliance costs as a proportion of the amount raised, if the issuer discovers during the offering process that there is greater investor interest in the offering than initially anticipated or if the cost of capital is lower than initially anticipated. As an alternative, we could have limited the maximum oversubscription amount to a certain percentage of the target offering amount, as suggested by one commenter.[1466] However, such a restriction might reduce valuable flexibility and potentially limit capital formation without appreciably enhancing investor protection.

The final rules do not require issuers to set a fixed price, as suggested by one commenter.[1467] While such an alternative might reduce an investor's cost of evaluating the investment, it would reduce flexibility for issuers while providing only limited benefits to investors in light of other disclosures required in the final rules. Further, the required disclosure

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1465 *See* Rule 201(h) of Regulation Crowdfunding. *See also* Section II.B.6.a above.

1466 *See* Joinvestor Letter; RFPIA Letter.

1467 *See* RocketHub Letter.

of the pricing method used and the final prices for the securities before an offering closes,[1468] coupled with the investor's ability to cancel his or her investment commitment,[1469] can mitigate potential concerns that dynamic pricing can be used to provide preferential treatment to certain investors (*e.g.*, when an issuer offers better prices to relatives or insiders). We also believe that the cancellation rights afforded by the rules will help to address the concerns about time pressure on the investment decision because investors will have the opportunity to cancel their investment commitments if they decide to do so.

h. Types of Securities Offered and Valuation

The final rules do not limit the type of securities that may be offered in reliance on Section 4(a)(6). This provision gives issuers the flexibility to offer the types of securities that are most compatible with their desired capital structure and financing needs. Such flexibility may benefit issuers to the extent that capital structure decisions can be relevant for an issuer's firm value.

The final rules do not prescribe a method for valuing the securities but instead require issuers to describe the terms of the securities and the valuation method in their offering materials. The required disclosure of valuation method is intended to facilitate informed investment decisions. As an alternative, as suggested by commenters, we could have prescribed the use of particular valuation standards,[1470] required issuers to base the valuation of their securities on the price at which the issuer previously sold securities,[1471] or considered other standards designed to

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1468 *See* Rule 201(l) of Regulation Crowdfunding.

1469 *See* Rule 201(j) of Regulation Crowdfunding.

1470 *See, e.g.*, 11 Wells Letter; Active Agenda Letter; Borrell Letter; Ellenbogen Letter; Greer Letter; Mountain Hardwear Letter; Moyer Letter; NaviGantt Letter; Vidal Letter.

1471 *See, e.g.*, Public Startup Letter 3; Wefunder Letter.

ensure that securities are fairly valued and that approaches to valuation that put investors at a disadvantage are prohibited.[1472] If we required a specific valuation methodology, such as one of the suggested alternatives, and it were appropriate for a particular issuer, it could mitigate the likelihood of inaccurate valuations and result in more informed decisions by investors. However, specific valuation requirements that do not accommodate inherent differences among companies, particularly in light of the uncertainty related to the valuation of early-stage companies, might result in inaccurate valuations and less informed investor decisions. Also, potential additional calculations and analysis that might be required to implement a prescribed valuation methodology could impose additional costs on issuers, compared to letting issuers select a valuation method that fits the particular circumstances of their offering.

i. Restrictions on Resales

The statute and the final rules include restrictions on the transfer of securities for one year, subject to limited exceptions (*e.g.*, for transfers to the issuer of the securities, in a registered offering, to an accredited investor or to certain family members).[1473] As we discussed in the proposal, we believe that including such proposed restrictions is important for investor protection. By restricting the transfer of securities for a one-year period, the final rules give investors in a business a defined period to observe the performance of the business and to potentially obtain more information about the potential success or failure of the business before trading occurs. The final rules permit transfers to trusts controlled by, or held for the benefit of, covered family members.[1474] In a change from the proposed rules, the restrictions apply to any purchasers and

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1472 *See* Consumer Federation Letter.

1473 *See* Section 4A(e). *See also* Rule 501(a) of Regulation Crowdfunding.

1474 *See* Rule 501(a)(4) of Regulation Crowdfunding.

not only to the initial purchasers, consistent with the suggestions of commenters.[1475] This change addresses the possibility of the initial purchaser selling securities to an eligible purchaser and such eligible purchaser reselling them to the public within the first year, resulting in the securities becoming widely traded within the first year.

We recognize that resale restrictions will impose costs. The one-year restriction on transfers of securities purchased in a transaction conducted in reliance on Section 4(a)(6) may impede price discovery, raise capital costs to issuers and limit investor participation, particularly among investors who are unable or unwilling to risk locking up their investments for this period. The illiquidity cost resulting from the resale restriction may be mitigated, in part, by provisions that allow investors to transfer the securities within one year of issuance by reselling the securities to accredited investors, back to the issuer or in a registered offering or transferring them to certain family members or trusts of those family members. The effect of resale restrictions on the extent to which investors make informed investment decisions is unclear. While resale restrictions may disincentivize investors from continuing to gather and analyze information about the issuer after investing while the resale restrictions are in effect, resale restrictions may also strengthen the incentive to conduct due diligence on the issuer and gather and analyze information before the initial investment. Nevertheless, at the investment amounts involved in these transactions, a typical purchaser's incentives to gather and analyze information before or after investing likely will remain limited, regardless of the presence of resale restrictions.

4. Intermediary Requirements

The statute and the final rules require that offerings in reliance on Section 4(a)(6) be conducted through an intermediary that is a registered broker-dealer or registered funding portal.

[1475] *See* CrowdCheck Letter 3; Moskowitz Letter.

The use of a registered intermediary to match issuers and investors will cause issuers to incur certain transaction costs associated with the intermediation activity[1476] but also will provide centralized venues for crowdfunding activities that are expected to lower investor and issuer search costs. As discussed earlier, existing lending-based, reward-based, and donation-based crowdfunding platforms already engage in a large volume of transactions in North America,[1477] demonstrating that the use of platforms for crowdfunding may be familiar to investors and issuers.

We believe that existing non-securities-based crowdfunding platforms will initially be the primary funding portals in the securities-based crowdfunding market. The entry of registered broker-dealers and new funding portals in the securities-based crowdfunding market will increase competition among existing non-securities-based crowdfunding intermediaries and potentially lower the cost of intermediation to issuers. One commenter stated that it has "a serious concern with Broker/Dealers having an unfair advantage in the market, by already being regulated and registered with the Commission as well as FINRA. Therefore, they may be able to service the market well ahead of Portals." [1478]

We acknowledge that, to the extent that it may take less time and cost for registered broker-dealers to comply with the requirements of Regulation Crowdfunding as compared to funding portals, registered broker-dealers may be at a competitive advantage compared to new entities that seek to register as funding portals and enter the crowdfunding market. However, as we discuss below, the registration requirements for funding portals are tailored to the more limited

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1476 *See* Section III.B.3.a above for a discussion of intermediary fees.

1477 *See* Section III.A.3 above.

1478 *See* RocketHub Letter. Several other commenters expressed concern about funding portals being at a competitive disadvantage to registered broker-dealers. *See, e.g.,* Joinvestor Letter; City First Letter; Seed&Spark Letter; Guzik Letter 1.

scope of funding portal activities and are thus expected to result in a lower compliance cost for these entities. Further, the effective dates of the final rules are expected to provide time for funding portals to register and comply with the other requirements of Regulation Crowdfunding before crowdfunding offerings can occur.[1479] We recognize, however, that registered broker-dealers can retain a competitive advantage relative to funding portals due to their ability to engage in a wider range of activities in the securities-based crowdfunding market.[1480] In this regard we note that the final rules permit funding portals to compensate a registered broker-dealer and to receive compensation from a registered broker-dealer for services in connection with the funding portal's offer or sale of securities in reliance on Section 4(a)(6),[1481] which may enable funding portals to partly mitigate the impact of restrictions on funding portal activities in the statute and final rules. Moreover, even if funding portals remain at a competitive disadvantage to registered broker-dealers in the securities-based crowdfunding market, overall the expected participation of multiple registered broker-dealers as intermediaries in offerings in reliance on Section 4(a)(6) may nevertheless result in a considerable level of competition in the securities-based crowdfunding marketplace.

Both existing non-securities-based crowdfunding platforms and registered broker-dealers will need to invest resources to comply with the requirements of the statute and final rules. In addition, registered broker-dealers will need to develop Internet-based crowdfunding platforms while existing non-securities-based crowdfunding platforms will need to register as funding

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1479 The time period between the effective date of the final rules pertaining to funding portal registration as compared to the later effective date for rules governing crowdfunding offerings is expected to mitigate some of these effects. *See also* Section II.C.2.a above.

1480 *See also* note 607.

1481 *See* Rule 402(b)(7) and Rule 402(b)(8) of Regulation Crowdfunding. *See also* Section II.D.3.g.

portals or broker-dealers and modify their existing platforms to conform to the requirements of the statute and the final rules. Although the eventual extent of broker-dealer involvement in the securities-based crowdfunding market is difficult to estimate, we believe that some broker-dealers may acquire or form partnerships with funding portals to obtain access to a new and diverse investor base. In addition, some existing non-securities-based crowdfunding platforms may eventually form partnerships with registered broker-dealers or funding portals. It is challenging to exactly predict the future number of persons (or entities) who will register as either broker-dealers or funding portals to act as intermediaries in securities-based crowdfunding transactions. For purposes of the PRA,[1482] we estimate that intermediaries will number approximately 110, including approximately 10 intermediaries that will register as broker-dealers in order to engage in securities-based crowdfunding; approximately 50 intermediaries that are already registered as broker-dealers and that will choose to serve as crowdfunding intermediaries; and approximately 50 intermediaries that are not already registered as broker-dealers and that will register as funding portals.[1483] It is possible that the actual number of participants will deviate significantly from these estimates, and it is likely that there will be significant competition between existing crowdfunding venues and new entrants that may result in further changes in the number and types of intermediaries as the market develops and matures. It also is likely that there will be significant

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1482 *See* Section IV.B.2 and Section IV.B.3 below.

1483 These estimates are based, in part, on recent indications of interest, which may change as the market develops. According to FINRA, as of October 3, 2013, approximately 36 entities have submitted the voluntary Interim Form for Funding Portals to FINRA to indicate their intention to act as funding portals under Title III of the JOBS Act. *See* Press Release, Financial Industry Regulatory Authority, FINRA Issues Voluntary Interim Form for Crowdfunding Portals (Jan. 10, 2013), *available at* http://www.finra.org/Newsroom/NewsReleases/2013/P197636; Financial Industry Regulatory Authority, *Crowdfunding Portals*, *available at* http://www.finra.org/industry/issues/crowdfunding. Based on these recent indications of interest, we expect that the number of funding portals that will ultimately register with the Commission will be approximately 50.

We note that these estimates are the same as the estimates of potential crowdfunding intermediaries set forth in the Proposing Release. We did not receive comments about these estimates.

developments in the types and ranges of crowdfunding products and services offered by intermediaries to potential issuers and investors, particularly as competitors gain additional experience in this new marketplace. Moreover, the business models of successful crowdfunding intermediaries are likely to change over time as they grow in size or market share or if they are forced to differentiate from other market participants in order to maintain their position in the market.

As a result of the uncertainty over how the market may develop, any estimates of the potential number of market participants, their services or fees charged are subject to significant estimation error. While we recognize that there are benefits as well as costs associated with the statutory requirements and the final rules pertaining to intermediaries, there are significant limitations to our ability to estimate these potential benefits and costs.

The statute requires that the offer or sale of securities in reliance on Securities Act Section 4(a)(6) be conducted through a broker-dealer or a funding portal that complies with the requirements of Securities Act Section 4A(a).[1484] Among other things, the intermediary must register with the Commission as a broker-dealer or a funding portal, and it also must register with a registered national securities association.[1485] The final rules implement these statutory requirements, including by requiring an intermediary to be a member of FINRA or any other applicable registered national securities association.

While the benefits and costs are described in further detail below, the following tables summarize the estimated direct costs to intermediaries, including broker-dealers and funding portals. Some of the direct costs of the rules will be incurred by all intermediaries, while others

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1484 *See* Section 4(a)(6)(C).

1485 *See* Section 4A(a)(2).

are specific to whether the intermediary is a new entrant (registering as a broker-dealer or a funding portal) or is already registered as a broker-dealer.

Although we have attempted to estimate the direct costs of the statute and the final rules on intermediaries, we recognize that some costs can vary significantly across intermediaries, and within categories of intermediaries. For example, some intermediaries may choose to leverage existing platforms or systems and so may not need to incur significant additional expenses to develop a platform or comply with specific requirements of Regulation Crowdfunding. In the Proposing Release we provided cost estimates for the various intermediary requirements and requested comment on our estimates. Several commenters discussed the estimates of the costs associated with intermediaries or provided cost estimates of their own.[1486] Below we discuss the comments received on each of these costs and any revisions to our estimates made in response.

We estimate that the cost for an entity to register as a broker-dealer and become a member of a national securities association in order to engage in crowdfunding pursuant to Section 4(a)(6) will be approximately $275,000, with an ongoing annual cost of approximately $50,000 to maintain this registration and membership.[1487] In addition, we estimate that the cost to comply

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1486 *See, e.g.*, ASSOB Letter (suggesting that the cost to establish a funding portal would run at least $480,000); Arctic Island Letter 8 (referring to the cost of establishing and managing escrow accounts); CapSchedule Letter (citing costs of managing securityholder records); Joinvestor Letter (suggesting in reference to records to be kept by funding portals that "[u]nder the expectation that crowdfunding portals will be online operations and will almost certainly retain records through digital methods, the burden of collection should be minimal" but not providing a specific estimate of the cost of compliance). Various commenters expressed concern with the cost imposed on intermediaries. *See, e.g.*, Heritage Letter (suggesting that the "costs incurred by the intermediary in dealing with an issuer, doing the required due diligence and background screening, establishing a web page describing the offering and so on do not vary linearly with the offering size"); Seed&Spark Letter; SBEC Letter (suggesting that there will be "extensive staff, technology and operational costs" in addition to the compliance costs estimated in the Proposing Release).

1487 We recognize that the cost of registering and becoming a member of a national securities association varies significantly among broker-dealers, depending on facts and circumstances. The cost can vary, among other factors, based on the number of associated persons of the broker-dealer entity and their licensing requirements, the scope of the brokerage activities, and the means by which the broker-dealer administers the registration process (*e.g.*, it may choose to hire outside counsel to assist with the process). We also

with the various requirements that apply to registered broker-dealers engaging in transactions pursuant to Section 4(a)(6) for these new registrants will be approximately $245,000 initially and approximately $180,000 in each year thereafter. In making this estimate, we assume that broker-dealers acting as intermediaries in transactions pursuant to Section 4(a)(6) will provide a full range of brokerage services in connection with these transactions, including certain services such as providing investment advice and recommendations, soliciting investors, and managing and handling customer funds and securities, that funding portals cannot provide.[1488]

If instead an entity were to register as a funding portal and become a funding portal member of a national securities association, we estimate the initial registration and membership cost will be approximately $100,000, with an ongoing cost of approximately $10,000 in each year thereafter to maintain this registration and membership.[1489] We estimate that the initial cost for a

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recognize that the time required for a broker-dealer to become a member of a national securities association varies and can take six months to one year. We estimate the range of this cost to be between $50,000 and $500,000, and so we have chosen the average amount of $275,000 for purposes of this analysis.

1488 Among other things, a broker-dealer providing recommendations and investment advice is required to comply with FINRA rules on suitability. *See* FINRA Rule 2111. A broker-dealer soliciting through advertisements is required to comply with FINRA rules relating to communications with the public. *See* FINRA Rule 2210. Broker-dealers handling customer funds and securities also are required to maintain net capital, segregate customer funds and comply with Exchange Act Rule 15c2-4. *See* Exchange Act Rules 15c3-1, 15c3-3 and 15c2-4 [17 CFR 240.15c3-1, 15c3-3 and 15c2-4].

1489 In making these estimates, we assume that the membership process will take approximately sixty days and that there will be no related licensing requirement for associated persons of the funding portal. In the Proposing Release, we estimated that the membership process will take approximately one month. While it does not affect our estimate of direct costs, we note that a longer membership process can result in incremental indirect costs to funding portals (e.g., opportunity costs due to not being able to serve as an intermediary in crowdfunding offerings while registration requirements are not met and competitive costs due to requiring additional time to register compared to registered broker-dealers. The time period between the effective date of the final rules pertaining to funding portal registration as compared to the later effective date for rules governing crowdfunding offerings is expected to mitigate these effects.

We also only include domestic entities in these estimates, which do not need to comply with the requirements in Regulation Crowdfunding that apply to nonresident funding portals. Nonresident funding portals are subject to an additional cost of completing Schedule C to Form Funding Portal, hiring and maintaining an agent for service of process and providing the required opinion of counsel. *See* Section IV.C.2.a. below (discussing burden estimates of these additional requirements for purposes of the PRA).

registered funding portal to comply with the requirements of the final rules will be approximately $67,000, with an ongoing cost of approximately $40,000 in each year thereafter.

Finally, we estimate that the incremental initial cost for an intermediary that is already registered as a broker-dealer to comply with the requirements of the final rules will be approximately $45,000, with an ongoing cost of approximately $30,000 in each year thereafter.

These estimated costs are consistent with those set forth in the Proposing Release and are exclusive of the cost of establishing and maintaining a platform and related functionality. For purposes of the PRA, we estimate that for the average intermediary, the mid-range initial external platform development cost will be approximately $425,000 and the ongoing cost will be approximately $85,000 per year.[1490] However, we anticipate considerable variation among intermediaries depending on whether they already have in place platforms and systems that can be adapted to meet the requirements of the final rules. We expect that intermediaries (whether broker-dealers or funding portals) that already have in place platforms and related systems that will need only to tailor their existing platform and systems to comply with the requirements of Regulation Crowdfunding, resulting in a lower initial cost on average of $250,000. We expect the ongoing cost to remain approximately $85,000 per year for an intermediary that already has in place a platform and related systems. Commenters did not provide estimates of the cost of establishing a platform or tailoring an existing platform to comply with the requirements of Title III. One commenter suggested that the cost of operating a funding portal and regulatory

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[1490] These estimates are based on intermediaries that use a third party to develop the platform. Intermediaries that develop the platform in-house may incur lower costs. For purposes of the PRA, we estimate that intermediaries that develop the platform in-house instead of using a third-party provider will spend an average of 1,500 hours for initial planning, programming and implementation and 300 hours per year in ongoing internal burden. For purposes of the PRA we estimate that approximately half of the intermediaries will use a third party to develop the platform and the other half will develop their platforms in-house. *See* Section IV.C.2.b below.

compliance would be at least $480,000 per year but did not break out this estimate into separate cost components.[1491]

Estimated Costs of Final Rules for Intermediaries that Register as Broker-Dealers

	Estimated Costs	
	Initial Cost (Year 1)	**Ongoing Cost per Year**
Form BD Registration and National Securities Association Membership	$275,000	$50,000
Complying with Requirements to Act as an Intermediary in, and to Engage in Broker-Dealer Activities Related to, Transactions pursuant to Section 4(a)(6)[1492]	$245,000	$180,000
Platform Development[1493]	$425,000	$85,000
Total	*$945,000*	*$315,000*

Estimated Costs of Final Rules for Intermediaries that Register as Funding Portals

	Estimated Costs	
	Initial Cost (Year 1)	**Ongoing Cost per Year**
Form Funding Portal Registration and National Securities Association Membership[1494]	$100,000	$10,000
Complying with Requirements to Act as an Intermediary[1495] in Transactions pursuant to Section 4(a)(6)	$67,000	$40,000
Platform Development[1496]	$425,000	$85,000

1491 *See* ASSOB Letter.

1492 As discussed above, these costs include, among others, the costs to the broker-dealer of having associated persons who have licensing requirements, suitability requirements, requirements relating to advertisements, net capital requirements, and compliance with Exchange Act Rule 15c2-4 (17 CFR 240.15c2-4), as well as the costs of complying with Subpart C of Regulation Crowdfunding. *See* Section IV.C. 2 below for further detail on our estimates, for PRA purposes, of the costs associated with the requirements under Subpart C.

1493 *See* Section IV.C.2.b below for further detail on our estimates, for PRA purposes, of the costs of developing a platform.

1494 As described above, this estimate reflects a streamlined process of becoming a member of a national securities association, which we assume will take approximately sixty days and not involve application or licensing of associated persons.

1495 This includes the costs of complying with the requirements of Subparts C and D of Regulation Crowdfunding. *See* Section IV.C.2 below for further detail on our estimates, for PRA purposes, of these costs.

1496 *See* Section IV.C.2.b below for further detail on our estimates, for PRA purposes, of the costs of developing a platform.

	Estimated Costs	
	Initial Cost (Year 1)	**Ongoing Cost per Year**
Total	*$592,000*	*$135,000*

Estimated Incremental Costs of Final Rules for Intermediaries Already Registered as Broker-dealers

	Estimated Costs	
	Initial Cost (Year 1)	**Ongoing Cost per Year**
Complying with Requirements to Act as an Intermediary in Transactions pursuant to Section 4(a)(6)[1497]	$45,000	$30,000
Platform Development[1498]	$425,000	$85,000
Total	*$470,000*	*$115,000*

Commenters suggested that funding portals should not be required to register with the Commission or become FINRA members (or members of any other registered national securities association), because unlike broker-dealers, they serve only as an "information delivery service."[1499] One commenter stated that the Commission's estimates in initial costs of registration as a funding portal and for ongoing expenses create a significant burden given that potential funding portals operate on modest budgets and with thin margins.[1500] As we note above, however, registration is a statutory requirement under Securities Act Section 4A(a)(1).[1501] While the registration requirements will necessarily impose costs on intermediaries, we believe they also will be effective in providing investor protection for the crowdfunding market while taking into

1497 This includes the incremental costs of complying with the requirements of Subpart C of Regulation Crowdfunding, but it excludes any registration or membership requirements. *See* Section IV.C.2 below for further detail on our estimates, for PRA purposes, of these costs.

1498 *See* Section IV.C.2.b below for further detail on our estimates, for PRA purposes, of the costs of developing a platform.

1499 *See* Perfect Circle Letter.

1500 *See* Seed&Spark Letter.

1501 *See* Section II.C.2.a above.

account the more limited activities of funding portals. Among other things, in addition to the Commission's oversight and rulemaking functions with regard to broker-dealers, FINRA currently is responsible for conducting most broker-dealer examinations, mandating certain disclosures by its members, writing rules governing the conduct of its members and associated persons, and informing and educating the investing public. Similarly, we believe that in addition to the benefits of the Commission's oversight with regard to funding portals, the regulatory framework that a registered national securities association – initially FINRA – will be required to create for funding portals will play an important role in the oversight of these entities.

The estimated costs in the tables above reflect the direct costs that intermediaries will incur in connection with registering as a broker-dealer on Form BD or as a funding portal on Form Funding Portal, submitting amendments to registrations and withdrawing registrations. For the purposes of the PRA, we estimate that approximately 50 intermediaries will be broker-dealers that have already registered with the Commission[1502] and, as such, these broker-dealers will not incur additional SEC registration costs associated with the final rules. Additionally, intermediaries that are not otherwise registered with FINRA or any other registered national securities association will need to register, and the estimated cost for such registration is included in the tables above. We anticipate that the cost for a funding portal to become a member of a registered national securities association will be lower than the cost for a broker-dealer to do so because of the more limited nature of a funding portal's permissible activities and the streamlined set of rules that an association is likely to impose on funding portals. In this regard, we note that FINRA has solicited

[1502] *See* Section IV.C.2 below.

public comment on a set of proposed rules and related forms for registered funding portals that become FINRA members pursuant to the crowdfunding provisions of the JOBS Act.[1503]

The final rules also require that an intermediary execute transactions exclusively through its online platform. This requirement may lower the potential for abusive sales practices. However, it may also prevent investors who lack Internet access from investing through crowdfunding, as suggested by one commenter.[1504] We believe that the use of an online platform will enhance the ability of issuers and investors to communicate transparently as compared to the alternative of allowing transactions to occur offline. This requirement also is expected to help issuers gain exposure to a wide range of investors, who also may benefit from having numerous investment opportunities aggregated in one place, resulting in lower search costs or burdens related to identifying suitable investment opportunities.

The final rules further require that an issuer conduct an offering or concurrent offerings in reliance on Section 4(a)(6) using a single intermediary.[1505] We recognize that this requirement may impose costs by limiting the set of investors, as well as communication about a transaction, to the extent that some investors do not use a specific crowdfunding platform.[1506] However, it may also enhance communication between issuers and investors, as suggested by some commenters,[1507] and enable investors to access investor discussions about a particular transaction

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1503 *See* Proposed Funding Portal Rules, *available at* http://www.finra.org/sites/default/files/NoticeAttachment/p369763.pdf. *See also FINRA Requests Comment on Proposed Funding Portal Rules and Related Forms*, FINRA Regulatory Notice 13-34, *available* at http://www.finra.org/sites/default/files/NoticeDocument/p370743.pdf. ("The rule is based on the current NASD Rule 1010 Series membership rules that apply to broker-dealers. However, the process for funding portals is simplified to reflect the limited nature of their business.")

1504 *See, e.g.*, Projecteureka Letter.

1505 *See* Instruction 1 to Rule 100(a)(3) of Regulation Crowdfunding. *See also* Section II.A.3.

1506 *See, e.g.*, Graves Letter.

1507 *See, e.g.*, CFA Institute Letter; RocketHub Letter.

on a single platform. This requirement may also reduce the risk of issuers circumventing the aggregate offering limit.

Some commenters suggested that the statutory and rule requirements for establishing a funding portal and ongoing maintenance and compliance expenses create a significant burden on funding portals.[1508] Among other concerns, commenters highlighted potential liability for intermediaries[1509] under Securities Act Section 4A(c) and the cost of conducting background checks[1510] pursuant to Rule 301(c) as particularly burdensome for funding portals. We are mindful of the potentially significant costs as a percentage of offering size incurred by intermediaries, especially funding portals, in securities-based crowdfunding offerings. However, intermediary requirements are designed to provide a measure of investor protection from the risk of fraud in small offerings by relatively unknown issuers. Concentration of certain due diligence tasks at the intermediary level may yield efficiency gains relative to having each small investor incur the cost to perform such tasks. In addition, although funding portals may be subject to issuer liability, the changes we have implemented in the final rules will give them greater ability to control which issuers conduct offerings on their platforms and thus to mitigate to some degree the risks of liability arising from such offerings.

a. Disclosure and Dissemination Requirements

The statute and final rules include disclosure and dissemination provisions designed to provide information to security-based crowdfunding investors. These provisions, together with

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1508 *See, e.g.*, ASSOB Letter (suggesting that the cost to establish a funding portal could be at least $480,000).

1509 *See, e.g.*, ABA Letter; AngelList Letter; BetterInvesting Letter; CFIRA Letter 10; City First Letter; EarlyShares Letter; EMKF Letter; FSI Letter; Graves Letter; Guzik Letter 1; IAC Recommendation; Inkshares Letter; Milken Institute Letter; PPA Letter; RocketHub Letter; SBA Office of Advocacy Letter; SBEC Letter; SeedInvest Letter 3; Seyfarth Letter; StartupValley Letter; Wefunder Letter; Winters Letter. *See also* Section II.E.5.

1510 *See, e.g.*, RocketHub Letter; Anonymous Letter 4; Zhang Letter. *See also* Section II.C.3.c above.

the issuer disclosure provisions discussed above, are expected to limit information asymmetries and promote the efficient allocation of capital amongst crowdfunding offerings. These provisions also will provide information intended to ensure that investors are aware of the risks associated with their investment, which can enhance investor protection. As discussed above, many of the costs and benefits of these provisions are difficult to quantify or estimate with any degree of certainty, especially considering that securities-based crowdfunding will constitute a new method for raising capital in the United States. Although we are not able to quantify the direct costs specifically associated with each of these requirements, these costs are reflected in our general estimates of the initial and ongoing costs for intermediaries to register, comply with their obligations under the final rules and develop a crowdfunding platform, as reflected in the tables above.

The final rules prohibit an intermediary or its associated persons from accepting an investment commitment until the investor has opened an account with the intermediary and the intermediary has obtained the investor's consent to electronic delivery of materials.[1511] This requirement will help ensure that certain basic information about the investor is on file with the intermediary and that all investors are on notice of the primary method of delivery for communications from the intermediary. To the extent that an intermediary uses a third party to establish account opening functionality, the costs relevant to this requirement will be incorporated into the cost to develop the platform.[1512]

The statute requires intermediaries to provide disclosures related to risks and other investor education materials. The final rules implement this statutory mandate by requiring intermediaries

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[1511] *See* Rule 302(a) of Regulation Crowdfunding.

[1512] *See also* Section IV.C.2.d below.

to deliver educational materials that explain how the offering process works and the risks associated with investing in crowdfunding securities.[1513] The educational requirements will help make investors aware of the limits and risks associated with purchasing crowdfunding securities and facilitate the selection of investments suited to their level of risk tolerance. They also may help ensure that offerings proceed more efficiently as investors will be better informed by the time they decide to make their investment commitments and receive required notices. However, we recognize that the effectiveness of the educational materials in enhancing investor protection will vary depending upon the quality of the educational materials and the education and experience of retail investors.[1514] In addition, materials that highlight the risks of securities-based crowdfunding can discourage investor participation, which may limit potential capital formation.

Under the final rules, the educational materials can be in any electronic format, including video format, and the intermediary will have the flexibility to determine how best to communicate the contents of the educational material. Accordingly, the cost for intermediaries to develop educational materials is expected to vary widely. For purposes of the PRA, we estimate that the initial cost for an intermediary using a third-party firm to develop and produce educational materials will be approximately $10,000 to $30,000 and the ongoing cost will be approximately $5,000 to $15,000 per year.[1515]

1513 *See* Rule 302(b) of Regulation Crowdfunding.

1514 *See* Jennifer E. Bethel and Allen Ferrell, *Policy Issues Raised by Structured Products*, HARV. L. & ECON. Discussion Paper No. 560, 2007, *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=941720.

1515 For the purposes of the PRA, we estimate that development of educational materials in-house will be associated with an average initial burden of approximately 20 hours and an average annual burden of approximately 10 hours. *See* Section IV.C.2.e below.

The final rules also require that intermediaries obtain representations from investors about their review of the investor education materials and their understanding of the risks.[1516] This requirement is expected to improve investors' understanding of investments in securities-based crowdfunding offerings. The direct costs of this requirement to an intermediary are reflected in the tables above as part of the costs of developing a crowdfunding platform, and we believe that the ongoing burden to comply will be minimal after the intermediary has systems in place to obtain such representations. This requirement also may limit capital formation to the extent that it deters investors from making investment commitments or otherwise participating in offerings made in reliance on Section 4(a)(6).

Under the final rules, an intermediary must clearly disclose the manner in which the intermediary is compensated in connection with offers and sales of securities in reliance on Section 4(a)(6).[1517] As explained above, we believe that investors will benefit by having information about how intermediaries are compensated, such as through compensation arrangements with affiliates. We believe that the costs of complying with this requirement generally will be included in the overall cost for intermediaries to develop their platforms, as it will entail adding an item of disclosure to the functionality of their platforms.[1518] While the requirement to disclose compensation arrangements may give rise to indirect costs due to the intermediary's competitors learning about the compensation arrangements, we do not expect such indirect costs to be significant since the intermediary's competitors can generally infer information about the intermediary's compensation arrangements from other sources.

[1516] *See* Rule 303(b)(2) of Regulation Crowdfunding.

[1517] *See* Rule 302(d) of Regulation Crowdfunding.

[1518] *See also* Section IV.C.2.f below.

The statute and the final rules further require that intermediaries make available certain issuer-provided information.[1519] We recognize that requiring intermediaries to provide prospective investors with information about the issuer will impose costs. We expect that intermediaries will incur costs to develop the functionality that will allow the uploading and downloading of issuer information. We believe that the direct costs of complying with this requirement will be included in the overall cost to intermediaries to develop their platforms and that this requirement will impose only nominal incremental costs on intermediaries on an ongoing basis, primarily because the functionality necessary to upload the required issuer disclosure information is a standard feature offered on many websites and would not require frequent updates.[1520]

The issuer disclosure requirements are expected to benefit investors by enabling them to better evaluate the issuer and the offering. Requiring intermediaries to make the issuer information publicly available and easily accessible on their platforms will reduce information asymmetries between issuers and investors and will enhance both transparency and efficiency of the crowdfunding market. Greater accessibility of issuer information may reduce incremental costs to investors of locating issuer information and may increase their willingness to participate in a securities-based crowdfunding offering, thereby enhancing capital formation.

The final rules also require an intermediary to provide communication channels on its platform, meeting certain conditions, which will allow investors who have opened accounts with intermediaries and representatives of the issuer to interact and exchange comments about the

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1519 *See* Rule 303(a) of Regulation Crowdfunding.

1520 *See also* Section IV.C.2.g below.

issuer's offering on that intermediary's platform, and which will be publicly available for viewing (i.e., by those who may not have opened accounts with the intermediary).[1521]

Compared with the alternative of not requiring intermediaries to provide communication channels, we believe this requirement will allow investors, particularly those who may be less familiar with online social media, to participate in online discussions about ongoing offerings without having to actively search for such discussions on external websites. Moreover, the requirement that promoters be clearly identified on these channels will enhance transparency, allowing those investors that draw information from an intermediary's online platform to make potentially better informed investment decisions. The direct costs of this requirement are reflected in the tables above as part of costs of developing a crowdfunding platform, and we believe that once the platform has been set up, the ongoing burden to comply will be minimal. We recognize, however, that this requirement will not assure that participants in online discussions on the intermediary's online platform convey accurate or relevant information in their postings, and it will not preclude investors from participating in discussions on external websites or other external social media.

The final rules also require intermediaries, upon receipt of an investment commitment from an investor, promptly to provide or send to the investor a notification of that investment commitment.[1522] This requirement will provide investors with key information about their investment commitments, including notice of the opportunity, as relevant, to cancel their investment commitments. Investors will benefit from these requirements because they will be provided with additional information with which to evaluate their investment commitments, their

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1521 *See* Rule 303(c) of Regulation Crowdfunding.

1522 *See* Rule 303(d) of Regulation Crowdfunding.

securities transactions and the intermediaries that are effecting those transactions. The direct costs of these requirements are reflected in the tables above as part of the costs of developing a crowdfunding platform.[1523]

The final rules implement the statutory requirement for intermediaries to allow investors to cancel their commitments to invest, by requiring investors to have until 48 hours prior to the deadline identified in the issuer's offering materials to cancel their investment commitments.[1524] If an issuer reaches its target offering amount prior to the target offering deadline, the final rules permit early closing of the offering under certain conditions, including a requirement that the intermediary send notices to investors informing them of the closing and the deadline for the opportunity to cancel.[1525] The final rules also set forth notice requirements and requirements related to the intermediary directing payments in the event of cancellations and material changes to offerings.[1526] Additionally, the final rules impose specific obligations on intermediaries related to informing investors about their right to cancel an investment commitment.[1527]

We believe that investors will benefit from receiving these notices because the notifications and accompanying information will keep investors informed about the status of the offering and thereby facilitate better investment decisions. This approach also will benefit investors by providing them with a specified period of time to review and assess information and communications about the issuer.

1523 *See also* Section IV.C.2.h below.

1524 *See* Rule 304(a) of Regulation Crowdfunding.

1525 *See* Rule 304(b) of Regulation Crowdfunding.

1526 *See* Rule 304(c) and Rule 304(d) of Regulation Crowdfunding.

1527 *See* Rule 302(b) of Regulation Crowdfunding.

We recognize that allowing investors to cancel their investment commitments up to 48 hours prior to the deadline identified in the issuer's offering materials may impose a cost on issuers who, because of investors cancelling commitments late in the offering period, may fall below the target offering amount and so decide to cancel the offering or to extend the offering period. Accordingly, we recognize that this requirement may reduce the overall amount of capital raised in offerings in reliance on Section 4(a)(6) and thus have an adverse effect on capital formation. Intermediaries are expected to incur direct costs in developing and maintaining systems to send the relevant notices to investors. These costs are reflected in the tables above as part of the cost of developing a crowdfunding platform.[1528]

b. Measures to Reduce the Risk of Fraud

The statute and final rules require intermediaries to have a reasonable basis for believing that an issuer seeking to offer and sell securities in reliance on Section 4(a)(6) through the intermediary's platform complies with the requirements in the final rules[1529] and has established means to keep accurate records of holders of the securities.[1530] Under the final rules, an intermediary must deny access to an issuer if it has a reasonable basis for believing that the issuer or the offering presents the potential for fraud or otherwise raises concerns about investor protection[1531] or that the issuer or any of its officers, directors (or any person occupying a similar status or performing a similar function) or 20 Percent Beneficial Owners was subject to a disqualification under the final rules.[1532] The intermediary also must conduct a background and

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1528 *See also* Section IV.C.2.h below.

1529 *See* Rule 301(a) of Regulation Crowdfunding.

1530 *See* Rule 301(b) of Regulation Crowdfunding.

1531 *See* Rule 301(c)(2) of Regulation Crowdfunding.

1532 *See* Rule 301(c)(1) of Regulation Crowdfunding.

securities enforcement check on each of these persons.[1533] We believe that these requirements will increase investor protection in connection with the offering.[1534]

As noted above, the specific costs and benefits of these provisions are difficult to quantify or estimate with any degree of certainty. However, we have attempted to reflect the direct costs of these provisions in the tables above as part of our general estimates for the cost of complying with requirements to act as an intermediary in transactions pursuant to Section 4(a)(6). For purposes of the PRA, the cost for an intermediary to fulfill the required background checks and securities enforcement regulatory history checks is estimated to be approximately $13,818 to $34,546 in the first year and approximately the same in subsequent years.[1535]

Each of these requirements is intended to help reduce the risk of fraud in securities-based crowdfunding. As a result of these requirements, investors will be able to rely on the efforts of the intermediary that conducted a background and securities enforcement check, solving a collective action problem that would be prohibitively costly if left to individual investors. To the extent that these checks help prevent fraudulent activity, they may increase investor willingness to participate in crowdfunding offerings, thereby facilitating capital formation. We anticipate that most intermediaries will employ third parties to perform these background checks.

We received several suggestions from commenters aimed at reducing or scaling the costs of the proposed requirements. One commenter suggested that the checks be required only after an issuer has met its target offering amount, so as to prevent unnecessary expense to the

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1533 *Id*.

1534 *See also* Section II.C.3 above.

1535 *See* Section IV.C.2.c below.

intermediary.[1536] Requiring a background check only after an issuer has reached its target may reduce the total cost of performing background checks for intermediaries; however, it also may result in intermediaries having to cancel offerings by issuers who fail the background checks, resulting in additional transactional and reputational costs for the intermediary. Overall, relative to this alternative, we believe that an intermediary performing a background check on an issuer prior to the securities offering will improve investor confidence in using a given intermediary.

While intermediaries are required to take certain steps to reduce the risk of fraud, the final rules provide intermediaries with the flexibility to decide the specific steps to take, consistent with some of the commenters' suggestions.[1537] We believe this may reduce intermediary costs relative to establishing a more stringent or more specific standard for intermediaries. For example, deeming an intermediary to have satisfied the Rule 301(b) requirement if the issuer has engaged the services of a transfer agent that is registered under Section 17A of the Exchange Act will reduce the intermediary cost while at the same time potentially improving investor protection.[1538] In addition, intermediaries may rely on the representations of the issuer unless they have reason to question the reliability of those representations. Overall, a more rigorous review requirement represents a tradeoff between enhanced investor confidence in the portal and higher compliance costs for intermediaries. We recognize that permitting an intermediary to rely on an issuer's representations unless the intermediary has reason to question the reliability of the representations can potentially lessen the incentive for an intermediary to thoroughly investigate the issuers and

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1536 Anonymous Letter 4.

1537 *See, e.g.,* StartupValley Letter; Vann Letter.

1538 We note that while for purposes of this provision, the issuer is not required to continue to engage the services of a registered transfer agent on an ongoing basis, since the use of a registered transfer agent is a condition for the Section 12(g) exemption, issuers with a large number of shareholders of record are expected to have an incentive to continue to engage the services of a registered transfer agent. *See* Section III.B.8. below.

securities to be offered on its platform. Such an outcome may result in higher levels of fraud compared to a requirement that intermediaries perform an independent investigation to ensure that the issuer complied with all the requirements. A higher level of fraud will negatively affect both investors in crowdfunding offerings and non-fraudulent issuers. While we recognize this potential adverse effect, we note that intermediaries may be subject to liability as "issuers," and this liability, together with potential reputational harm, is expected to provide significant incentives for intermediaries to monitor and investigate the offerings on their platforms. We also note that the communication channels provided on these platforms can provide a potential source of information for intermediaries, further facilitating their evaluation of prospective issuers.

c. Other Limitations on Intermediaries

The statute and final rules place certain limitations on intermediaries. These limitations are expected to increase investor protection in the securities-based crowdfunding market.

The final rules require an intermediary before accepting an investment commitment to have a reasonable basis for believing that an investor has not exceeded the final rules' investment limits but permit an intermediary to rely on investor representations concerning compliance unless the intermediary has reason to question the reliability of the representations.[1539] While we realize that investors may make inaccurate representations, we believe that this provision represents a reasonable approach to implement the statutory requirement, appropriately considering the need for investors to adhere to investment limitations while mitigating the costs incurred by intermediaries. The cost to update the required functionality for processing issuer disclosure and investor acknowledgment information is reflected in the tables above as part of the costs to

[1539] *See* Rule 303(b)(1) of Regulation Crowdfunding. *See also* Section II.C.5.b above.

develop a crowdfunding platform, and we believe that the ongoing burden to comply would be minimal.

Under the final rules, intermediaries must require any person, when posting a comment in the communication channels, to clearly disclose with each posting whether he or she is a founder or an employee of an issuer engaging in promotional activities on behalf of the issuer or a compensated promoter[1540] We believe that these disclosure requirements will benefit investors by promoting a transparent information sharing process. We further believe that intermediaries are in an appropriate position to take such steps as part of designing communication channels on their platform.

Under the final rules, intermediaries will incur direct costs in complying with the requirements to disclose compensation to promoters, and certain additional costs from time to time to ensure continued compliance. These costs are reflected in the table above as part of the costs of complying with the requirements to act as an intermediary in a Section 4(a)(6) transaction. In addition, if this requirement discourages the use of promoters by issuers, it may limit the investor pool for an offering made in reliance on Section 4(a)(6), thus limiting the ability of an issuer to raise capital.[1541]

The statute prohibits the directors, officers or partners of an intermediary, or any person occupying a similar status or performing a similar function, from having any financial interest in an issuer that uses the services of the intermediary. The final rules implement this statutory requirement. In a change from the proposed rules, the final rules provide exceptions to the prohibition on an intermediary having a financial interest in a crowdfunding issuer. The

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[1540] *See* Rule 303(c)(4) of Regulation Crowdfunding. *See also* Section II.C.5.c above.

[1541] *See* Rule 300(b) of Regulation Crowdfunding and Section II.C.2.b.

intermediary may hold a financial interest in the crowdfunding issuer if the financial interest represents compensation for the services provided to or for the benefit of the issuer in connection with the offer or sale of securities in a crowdfunding offering and consists of securities of the same class and having the same terms, conditions and rights as the securities being offered or sold in the crowdfunding offering through the intermediary's platform. By not extending the prohibition from having any financial interest in an issuer to intermediaries in all instances, the final rules allow for more flexibility in the payment arrangements between issuers and intermediaries. This additional option by which the issuer may pay an intermediary for its services may be beneficial for issuers by allowing them to use more of the capital raised in an offering for future investments rather than paying a portion of it as a fee to the intermediaries. It also allows funding portals to share in the upside of successful issuers, generating potentially larger revenue than the offering fee. While allowing intermediaries to have a financial interest in issuers can align incentives between intermediaries and investors,[1542] it can alternatively lead to potential conflicts of interest between intermediaries and investors.[1543] While we believe that such conflicts of interest are possible and may reduce investor protection, they will be significantly mitigated by the requirement that an intermediary's financial interest in an issuer consist of securities of the same class and having the same terms, conditions and rights as the securities being offered or sold in the crowdfunding offering through the intermediary's platform. Such limitations on an intermediary's financial interest, combined with reputational concerns and the

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1542 *See, e.g.,* AngelList Letter ("So long as the program was consistently applied without judgment by the intermediary, the net effect would purely be to align the interests of the intermediary with the investor."). *See also* EMKF Letter; Hackers/Founders Letter; Heritage Letter; Milken Institute Letter; RoC Letter; RocketHub Letter; Thomas Letter 1.

1543 *See* Jacobson Letter.

accompanying disclosure requirements, will likely curb the incentives of intermediaries to act in a way that harms the interests of crowdfunding investors.

The statute requires that intermediaries ensure that all offering proceeds are provided to the issuer only when the aggregate capital raised from all investors is equal to or greater than a target offering amount.[1544] The final rules implement this requirement by requiring intermediaries that are registered as broker-dealers to comply with the existing requirements of Exchange Act Rule 15c2-4 and by requiring intermediaries that are registered funding portals to direct investors to transmit the funds or other consideration directly to a qualified third party that has agreed in writing to hold the funds for the benefit of the investors and the issuer and to promptly transmit or return the funds to the persons entitled to such funds.[1545] Based on several commenters' suggestions,[1546] we modified the proposed definition of qualified third parties in Rule 303(e) also to include registered broker-dealers that carry customer or broker or dealer accounts and hold funds or securities for those persons and credit unions insured by the NCUA.[1547] The final rules also require a funding portal to direct the qualified third party to transmit funds to the issuer once the target offering amount is reached and the cancellation period has elapsed; to return funds to an investor when an investment commitment has been cancelled; and to return funds to investors when the offering has not been completed.

These requirements will benefit investors and issuers by helping ensure that funds are appropriately refunded or transmitted in accordance with the terms of the offering. In particular, the requirement that the account in which funds are deposited be exclusively for the benefit of

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1544 *See* Section 4A(a)(7).

1545 *See* Rule 303(e) of Regulation Crowdfunding.

1546 *See, e.g.*, Growthfountain Letter; Vann Letter; Ex24 Letter; FOLIOfn Letter.

1547 *See* Rule 303(e) of Regulation Crowdfunding. *See also* Section II.C.5.b above.

investors and the issuer will help prevent the intermediary or other parties from claiming or otherwise unlawfully appropriating funds from that account. Expanding the definition of "qualified third parties" will increase the number of third parties available to hold funds in an escrow or in an account for the benefit of investors and the issuer, potentially reducing the cost of the service due to increased competition. We do not expect any significant costs due to this change from the proposed rules because credit unions insured by the NCUA offer similar protections to banks while registered broker-dealers that carry customer or broker or dealer accounts and hold funds or securities for those persons are subject to various regulatory obligations, which are designed to provide protection of investor funds through the imposition of capital and other requirements.[1548]

Under the statute, intermediaries may not compensate promoters, finders or lead generators for providing broker-dealers or funding portals with the personally identifiable information of any potential investor. The final rules implement this statutory requirement by prohibiting an intermediary from compensating any person for providing the personally identifiable information of any crowdfunding investor to intermediaries.[1549] Investors will benefit from the privacy protection provided by this prohibition. Intermediaries will incur a cost because the rule will not allow them to use personally identifiable information to target and seek out specific investors, thus reducing the potential investor pool for certain offerings. However, subject to this restriction, the final rules permit an intermediary to compensate a person for directing issuers or investors to the intermediary's platform in certain situations.[1550] This

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[1548] *See* note 868.

[1549] *See* Rule 305(a) of Regulation Crowdfunding.

[1550] *See* Rule 305(b).

provision will provide intermediaries with an alternative means to attract more investors to their crowdfunding platforms, thereby mitigating some of the costs associated with the restriction on paying for personally identifiable information.

5. Additional Funding Portal Requirements

Under the final rules, a funding portal must register with the Commission by filing a complete Form Funding Portal with information concerning the funding portal's operation.[1551] The final rules also include the statutory requirement that a funding portal be a member of a registered national securities association. In the table above, we estimate the costs that intermediaries will incur related to registering as a funding portal on Form Funding Portal and becoming a member of a national securities association to be approximately $100,000 in the initial year and $10,000 thereafter.

The requirement that funding portals register with the Commission and become a member of a national securities association will benefit investors by providing regulatory oversight for these new entities, which will help to reduce the risk for fraud. Although there are costs associated with this requirement, we believe that the protections deriving from this requirement will benefit investors, issuers and potentially intermediaries by helping to create a marketplace in which investors are more willing to participate and issuers are more comfortable using this method of capital formation.

The final rules also require that funding portals use Form Funding Portal to provide updates whenever information on file becomes inaccurate for any reason, to register successor funding portals and to withdraw from funding portal registration. Although funding portals would incur time and compliance costs to update Form Funding Portal, we expect funding portals will

[1551] *See* Rule 400(a) of Regulation Crowdfunding.

have experience with the filing process for Form Funding Portal from their registration and, as a result, will be familiar with the filing process by the time they update the form. In the tables above, this cost is reflected in the $10,000 annual compliance cost associated with registering on Form Funding Portal and becoming a member of a registered national securities association.

The final rules allow nonresident funding portals to register with the Commission, provided that certain conditions are met.[1552] The final rules require a nonresident funding portal to appoint an agent for service of process in the United States and to certify both that it can, as a matter of law, and will provide the Commission and any national securities association of which it becomes a member with prompt access to its books and records and submit to onsite inspection and examination by the Commission and the national securities association. The funding portal also must provide an opinion of counsel attesting to the funding portal's ability to comply with these requirements under home country law. As discussed above, the final rules condition nonresident funding portal registration on the presence of an information sharing arrangement between the Commission and the regulator in the funding portal's jurisdiction.[1553] This provision is expected to facilitate Commission oversight of registered nonresident funding portals, with the potential benefit of stronger protection of investors in offerings conducted on such portals. However, it may limit the ability of some nonresident funding portals to register, potentially resulting in adverse competitive effects on nonresident portals in jurisdictions without an information sharing agreement.

Compared to the alternative of not allowing nonresident entities to operate as funding portals in the U.S. crowdfunding market, the final rules may increase competition among

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[1552] *See* Rule 400(f) of Regulation Crowdfunding.

[1553] *See* Rule 400(f) of Regulation Crowdfunding.

crowdfunding intermediaries, which in turn may reduce the fees that intermediaries charge to issuers. Lower costs of raising capital can also attract more potential issuers to the crowdfunding market, thus enhancing capital formation. Due to lack of data, we are not able to estimate the magnitude of these potential effects.

Although the requirements with respect to the appointment of an agent for service of process, a certification and a legal opinion will impose costs on nonresident funding portals, these requirements are expected to enhance investor protection by requiring steps designed to ensure that the books and records of funding portals that are not based in the United States, or that are subject to laws other than those of the United States, nevertheless are accessible to the Commission and other relevant regulators for purposes of conducting examinations of, and enforcing U.S. laws and regulations against these entities. For PRA purposes, we estimate that nonresident intermediaries will face an additional cost for outside professional services of $25,179 per intermediary to retain an agent for service of process and provide an opinion of counsel to register as a nonresident funding portal.[1554]

The statute also provides an exemption from broker-dealer registration for funding portals. The final rules implement the statutory requirement by stating that a registered funding portal is exempt from the broker-dealer registration requirements of Exchange Act Section 15(a)(1) in connection with its activities as a funding portal.[1555] We believe this approach of exempting funding portals from broker-dealer registration and its accompanying regulations will benefit the market and its participants. The activities of funding portals will be more limited than those of

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[1554] For the purposes of the PRA, we estimate that entities that register as nonresident funding portals also will incur an additional internal burden of half an hour to complete Schedule C, half an hour to hire an agent for the service of process, and one hour to provide an opinion of counsel. *See* Section IV.C.2.a.

[1555] *See* Rule 401 of Regulation Crowdfunding.

broker-dealers. Thus, the final rules require funding portals to comply with registration requirements that are more appropriate for their limited, permissible activities, rather than the more extensive and higher cost requirements that accompany broker-dealer registration. Lower registration costs for funding portals may translate into lower fees charged to issuers that use these portals, thus possibly benefiting issuers of crowdfunding securities and potentially increasing capital formation. Due to lack of data, we are unable to quantify these potential benefits.

a. Safe Harbor for Certain Activities

Exchange Act Section 3(a)(80) prohibits funding portals from (1) offering investment advice or recommendations, (2) soliciting purchases, sales or offers to buy securities offered or displayed on the funding portal's platform, (3) compensating employees, agents or other such persons for solicitation or based on the sale of securities displayed or referenced on the funding portal's platform, or (4) holding, managing, possessing or otherwise handling investor funds or securities. The final rules give funding portals, their associated persons, affiliates and business associates, a measure of clarity on activities that are permissible without violating these statutory prohibitions, while also helping to protect investors from activities that create potential conflicts of interest.[1556] Thus, compared with the alternative that we could have chosen, that of not providing the safe harbor, the safe harbor provisions in the final rules may facilitate regulatory compliance for funding portals, potentially with corresponding benefits for both issuers and investors. Some safe harbor provisions have additional benefits and costs, which we discuss below. Other safe harbor provisions may facilitate the implementation of other provisions of the final rules in instances where the crowdfunding intermediary is a funding portal, in which case the benefits and costs of such safe harbor provisions will be inseparable from the benefits and costs of

[1556] *See* Rule 402 of Regulation Crowdfunding.

the other provisions of the final rules as applied to instances where the crowdfunding intermediary is a funding portal.

The safe harbor for a funding portal to provide communication channels on its platform[1557] will facilitate the realization of the benefits of the provision in the final rules that requires the intermediary to provide communication channels on its platform[1558] in instances where the crowdfunding intermediary is a funding portal. The provision of communication channels by the funding portal has the potential to attract a greater number of investors to crowdfunding transactions through funding portals than otherwise would be the case, thereby encouraging capital formation. The provision of communication channels may enhance information sharing among investors, although the relevance and accuracy of the information shared by investors on these communication channels will likely vary from offering to offering.

In a change from the proposal, the final rules include a conditional safe harbor that will permit funding portals, consistent with the prohibitions under Exchange Act Section 3(a)(80), to determine whether and under what circumstances to allow an issuer to offer and sell securities in reliance on Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)) through their platforms.[1559] Allowing funding portals to decide which securities to offer through their platforms will potentially decrease compliance costs for funding portals because limiting the offerings available on their platform can help decrease the risk of statutory liability under Section 4A(c) of the Securities Act, consistent with the suggestions of some commenters.[1560] The ability to determine which issuers may offer and sell securities through their platforms may also make it easier for

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1557 *See* Rule 402(b)(4) of Regulation Crowdfunding.

1558 *See* Rule 303(c) of Regulation Crowdfunding.

1559 *See* Rule 402(b)(1) of Regulation Crowdfunding.

1560 *See e.g.,* CrowdCheck 2 Letter; Milken Institute Letter; RocketHub Letter. *See also* Section II.D.3.a.

funding portals to bar potentially fraudulent offerings from their platforms, thereby potentially enhancing investor protection, consistent with the suggestions of various commenters,[1561] as well as screen out offerings by issuers that are unprepared or not "crowdfund-ready."[1562] A reduction in the prevalence of potentially fraudulent offerings, in turn, may increase investor confidence and facilitate capital formation in the securities-based crowdfunding market. However, we recognize that, depending on the funding portal, the ability to exercise discretion with respect to which offerings to include on the platform may result in the exclusion of some issuers that do not pose a risk of fraud, potentially limiting capital formation and investor access to crowdfunding investment opportunities in those instances. This concern is expected to be mitigated, in part, by the reputational incentives of intermediaries and competition within the crowdfunding market. We also recognize that, while funding portals remain subject to more limitations concerning their activities in the crowdfunding market relative to registered broker-dealers, the ability to exercise discretion with respect to which offerings to include on their platforms is expected to partly mitigate the competitive disadvantage of funding portals relative to registered brokers, as suggested by several commenters.[1563]

The final rules also allow a funding portal to highlight particular issuers or offerings of securities made in reliance on Section 4(a)(6) on its platform based on objective criteria, for example: (1) the type of securities being offered (*e.g.*, common stock, preferred stock or debt securities); (2) the geographic location of the issuer; (3) the industry or business segment of the issuer; (4) the number or amount of investment commitments made; (5) the progress in meeting

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1561 *See e.g.*, ABA Letter; CrowdCheck 2 Letter; Graves Letter; Seyfarth Letter.

1562 *See* EMKF Letter; SBEC Letter.

1563 *See e.g.*, BetterInvesting Letter; EMKF Letter; SBA Office of Advocacy Letter; ABA Letter; CfPA Letter; CrowdCheck 2 Letter; Graves Letter; Seyfarth Letter; IAC Recommendation; CFIRA Letter 12.

the target offering amount or, if applicable, the maximum offering amount, and (6) the minimum or maximum investment amount.[1564] The final rules require that these criteria be objective and reasonably designed to highlight a broad selection of issuers and offerings and be applied consistently to all potential issuers and offerings. They also specify that such criteria may not be related to the advisability of investing in the issuer or offering and may not give the impression of an investment recommendation.[1565] Under the final rules, funding portals may provide search functions or other tools on its platform that users may use to search, sort or categorize available offerings according to objective criteria.[1566]

A funding portal may choose to categorize offerings into general subject areas or provide search functions that, for example, allowing an investor to sort through offerings based on a combination of different objective criteria. We believe that these safe harbor provisions will benefit investors by facilitating investor access to information about offerings characterized by certain broad, objective criteria, to the extent that funding portals provide such features and tools in reliance on the final rules. By enabling issuers to utilize technology to lower the costs of each investor to search for information about a particular category of offerings, these provisions also may enhance efficiency. To the extent that the availability of these features and tools encourages investor participation in crowdfunding offerings, these provisions may have a beneficial effect on capital formation in the crowdfunding market.

The final rules prohibit a funding portal from receiving any special or additional compensation for highlighting (or offering to highlight) one or more issuers or offerings on its

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1564 *See* Rule 402(b)(2) of Regulation Crowdfunding.

1565 *Id*.

1566 *See* Rule 402(b)(3) Regulation Crowdfunding.

platform.[1567] This prohibition is expected to benefit investors by helping prevent conflicts of interest and incentives for funding portals to favor certain issuers over others. The final rules also make clear that such objective criteria may not include the advisability of investing in the issuer or its offering or an assessment of any characteristic of the issuer, its business plan, its management, or risks associated with an investment.[1568]

Under the final rules, funding portals are permitted to provide advice to an issuer on the structure and content of its offerings, including assistance to the issuer in preparing offering documentation.[1569] This will allow issuers to obtain guidance that may not typically be available to them and thereby help to lower funding costs. Many potential issuers seeking to offer and sell crowdfunding securities are unlikely to be familiar with how to structure offerings so as to raise capital in the most cost effective manner, and they may not have the capital, knowledge or resources to hire outside advisors. Given that an issuer will be required to conduct its securities-based crowdfunding offerings through an intermediary, we believe that permitting funding portals to provide these services to issuers will lower overall transaction costs for issuers, as they will not need to engage additional parties to provide these services. This effect will in turn help enhance market efficiency.

The final rules also provide a safe harbor for a funding portal to compensate a third party for referring a person to the funding portal in certain circumstances.[1570] This enables funding portals to realize the benefits of the provision in the final rules that permits an intermediary to compensate a person for directing issuers or investors to the intermediary's platform in certain

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1567 *See* Rule 402(b)(2) of Regulation Crowdfunding.

1568 *See* Rule 402(b)(2) and Rule 402(b)(3) of Regulation Crowdfunding.

1569 *See* Rule 402(b)(5) of Regulation Crowdfunding.

1570 *See* Rule 402(b)(6) of Regulation Crowdfunding.

circumstances.[1571] This provision is expected to benefit intermediaries by providing them with a means to attract more investors to their crowdfunding platforms, thereby encouraging capital formation. Investors also will benefit from the condition of this safe harbor prohibiting transaction-based compensation (other than to registered broker-dealers), which is expected to reduce the incentive for abusive practices.

The final rules also provide a safe harbor for a funding portal to pay or offer to pay compensation to a registered broker-dealer for services provided in connection with the offer or sale of securities in reliance on Section 4(a)(6), subject to conditions set forth in the rule.[1572] Similarly, a funding portal can, subject to certain conditions, receive compensation from a registered broker-dealer for services provided in connection with the offer or sale of securities by the funding portal in reliance on Section 4(a)(6).[1573] We note that some commenters expressed concern that such relationships between funding portals and broker-dealers could create conflicts of interest.[1574] However, funding portals are expected to benefit from being able to enter into these types of arrangements with registered broker-dealers who can provide services that the funding portals otherwise are prohibited from providing, such as engaging a broker-dealer to serve as a qualified third party for the transmission of investor funds. Broker-dealers also will benefit from the additional business that funding portals may be able to attract through the funding portals' platforms, as well as from services, such as those related to technology, that funding portals can provide. We anticipate that these types of service arrangements will ultimately benefit investors.

1571 *See* Rule 305(b) of Regulation Crowdfunding.

1572 *See* Rule 402(b)(7) of Regulation Crowdfunding.

1573 *See* Rule 402(b)(8) of Regulation Crowdfunding.

1574 *See e.g.,* Commonwealth of Massachusetts Letter; RocketHub Letter.

The final rules permit a funding portal to advertise its existence and identify one or more issuers or offerings available through its platform subject to certain conditions.[1575] This provision will benefit funding portals by allowing them to potentially attract more investors to their crowdfunding platforms. This provision also may enhance market efficiency as investors become more aware of available offerings through advertisements by funding portals and are thus able to better match their investments with projects that are better suited to their risk preferences and investment strategies. The conditions on advertising by funding portals in the final rules aim to consider informational benefits and investor protection concerns. For instance, while a funding portal advertising its existence may also identify one or more issuers or offerings available on its platform, it must do so on the basis of objective criteria that are reasonably designed to identify a broad selection of issuers and offerings and are applied consistently to all potential issuers and offerings. In addition, advertisements sent by a funding portal must not suggest that it is a recommendation to purchase a security or advice as to the advisability in investing in any security.[1576] While we believe these conditions are appropriate to protect the integrity of the crowdfunding market, we recognize that they may impose costs on funding portals. For example these conditions may limit the utility of advertising for the funding portal while the prohibition on special or additional compensation for identifying the offering in an advertisement may reduce the funding portal's revenue.

As discussed above, the final rules require an intermediary to deny access to its platform to an issuer that the intermediary has a reasonable basis for believing presents the potential for fraud

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1575 *See* Rule 402(b)(9) of Regulation Crowdfunding.

1576 *See* Section II.D.3.h.

or otherwise raises concerns about investor protection.[1577] The final rules also provide a conditional safe harbor to intermediaries that are funding portals to deny access to the platform or cancel an offering in such instances.[1578] These provisions are expected to enhance investor protection by giving funding portals greater ability to deny potentially fraudulent offerings. Funding portals are expected to benefit from the ability to deny access to certain issuers to protect the integrity of the offering process and the market reputation of their crowdfunding platforms, without fear of violating the statutory prohibition on providing investment advice.

The final rules specify that a funding portal may accept, on behalf of an issuer, investment commitments for crowdfunding offerings from investors.[1579] Under the final rules funding portals also can direct investors where to transmit funds or remit payment in connection with the purchase of securities offered and sold in reliance on Section 4(a)(6).[1580] Similarly, a funding portal can direct a qualified third party to release proceeds of a successful offering to the issuer upon completion of the offering or to return investor proceeds when an investment commitment or offering is cancelled.[1581] These provisions will facilitate the implementation of the requirements of the final rules regarding the maintenance and transmission of investor funds[1582] for intermediaries that are funding portals and give both funding portals and entities with which they do business a measure of legal certainty that funding portals accepting investment commitments for crowdfunding offerings and providing direction for funds to and from qualified third parties in

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1577 *See* Rule 301(c) of Regulation Crowdfunding.

1578 *See* Rule 402(b)(10) of Regulation Crowdfunding.

1579 *See* Rule 402(b)(11) of Regulation Crowdfunding.

1580 *See* Rule 402(b)(12) of Regulation Crowdfunding.

1581 *See* Rule 402(b)(13) of Regulation Crowdfunding.

1582 *See* Rule 303(e) of Regulation Crowdfunding.

compliance with the final rules will not be in violation of the statutory prohibitions on holding, managing, possessing or otherwise handling investor funds or securities. While we agree with the commenter that stated that the requirement to use a qualified third party to handle customer funds creates an additional cost,[1583] Section 3(a)(80)(D) of the Exchange Act explicitly prohibits funding portals from handling customer funds and securities.

b. Compliance Requirements

The final rules require that a funding portal implement written policies and procedures, reasonably designed to achieve compliance with the federal securities laws and the rules and regulations thereunder, relating to its business as a funding portal.[1584] This requirement will provide a benefit to investors and funding portals alike, as written policies and procedures will enhance compliance with the final rules. Funding portals will incur costs associated with the requirement to develop their own procedures and implement written policies and procedures, as well as to update and enforce them. These costs are reflected in the tables above as part of the costs to comply with requirements to act as an intermediary in transactions pursuant to Section 4(a)(6).

In contrast to the proposal, the final rules do not impose anti-money laundering (AML) obligations for funding portals. Some commenters generally suggested that since funding portals are prohibited from handling customer funds and securities, they should not be required to comply with AML provisions.[1585] As noted above, we believe it would be appropriate to work with other

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1583 *See* Stephenson, *et al*., Letter.

1584 *See* Rule 403(a) of Regulation Crowdfunding.

1585 *See, e.g.,* PeoplePowerFund Letter; Public Startup Letter 3; RFPIA Letter.

regulators to develop consistent and effective AML obligations for funding portals.[1586] By not imposing AML requirements in the final rules, we may avoid the possibility of conflicting or overlapping requirements. Registered broker-dealers that serve as intermediaries in securities-based crowdfunding transactions continue to have AML obligations, as do certain other parties involved in transactions conducted pursuant to Section 4(a)(6), such as a bank acting as a qualified third party to hold investor funds.[1587] To the extent that this difference in compliance obligations between funding portals and registered broker-dealers affects compliance costs and persists in the future, it may place funding portals at a relative competitive advantage. If this difference in compliance obligations between funding portals and registered broker-dealers persists in the future, it may also potentially expose investors in those securities-based crowdfunding offerings for which the intermediary is a funding portal to additional risks.

Additionally, the statute requires that intermediaries take such steps to protect the privacy of information collected from investors as we determine appropriate. In the final rules, we implement this statutory provision by requiring a funding portal to comply with Regulation S-P, S-ID and Regulation S-AM, as they apply to broker-dealers.[1588] We recognize that compliance with these privacy requirements will impose costs on funding portals. However, we believe that requiring a funding portal to comply with privacy obligations will help protect the personally identifiable information of investors, consistent with how it is required to be protected by other financial intermediaries. These privacy protections can give investors the confidence to participate in offerings made in reliance on Section 4(a)(6), which will facilitate capital formation

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1586 *See* Section II.D.4.b.

1587 *Id.*

1588 *See* Rule 403(b) of Regulation Crowdfunding.

and benefit the markets generally. As an alternative, we could have developed a more limited privacy regime applicable only to funding portals. Such an alternative would result in inconsistent treatment of funding portals and broker-dealers with respect to privacy obligations and could reduce the willingness of investors to participate in securities-based crowdfunding offerings. This alternative might also affect competition between funding portals and registered broker-dealers in the market for securities-based crowdfunding offerings.

As a condition to exempting funding portals from the requirement to register as broker-dealers under Exchange Act Section 15(a)(1), Exchange Act Section 3(h)(1)(A) requires that registered funding portals remain subject to, among other things, the Commission's examination authority. Under the final rules, a funding portal is required to permit the examination and inspection of all its business and business operations relating to its activities as a funding portal, such as its premises, systems, platforms and records, by Commission representatives and by representatives of the registered national securities association of which it becomes a member.[1589] Although funding portals will face time and compliance costs in submitting to Commission and registered national securities association examinations, inspections or investigations, and potentially responding to any issues identified, funding portals, investors and issuers will benefit from the enhanced compliance with legal obligations due to this oversight, as well as the sanctions or other disciplinary actions that may follow upon findings of violations through such inspections, examinations or investigations.

Further, the final rules require a registered funding portal to maintain and preserve certain books and records relating to its business for a period of not less than five years and in an easily-

[1589] *See* Rule 403(c) of Regulation Crowdfunding.

accessible place for the first two years.[1590] Recordkeeping requirements can assist registrants with compliance. They are a well-established and important element of the approach to broker-dealer regulation, as well as the regulation of investment advisers and others, and are designed to maintain the effectiveness of our inspection program for regulated entities, facilitating our review of their compliance with statutory mandates and with our rules. These requirements will enable the Commission and registered national securities organizations to more effectively gather information about the activities in which a funding portal has been engaged to discern whether the funding portal and the other parties are in compliance with the requirements of Regulation Crowdfunding and other relevant regulatory requirements. Standardized recordkeeping practices for intermediaries will enable regulators to perform more efficient, targeted inspections and examinations and thereby increase the likelihood of identifying improper conduct at earlier stages of the inspection or examination, which ultimately will benefit investors and the marketplace as a whole. To the extent that these requirements result in better regulatory oversight, they may increase investor confidence in funding portals and may also benefit funding portals by promoting issuer reliance on funding portals in crowdfunding offerings.

Funding portals may incur costs in establishing the systems necessary to comply with the books and records requirements. We note that the records required to be made and preserved under the final rules are those that would ordinarily be made and preserved in the ordinary course of business by a regulated broker-dealer engaging in these activities. Entities that newly register as broker-dealers will be subject to the recordkeeping requirements of Rules 17a-3 and 17a-4.

1590 *See* Rule 404(a) of Regulation Crowdfunding. We note that registered broker-dealers already are required to comply with Exchange Act Rules 17a-3 and 17a-4 pertaining to books and records (17 CFR 240.17a-3 and 17a-4). Thus, all intermediaries, whether registered as broker-dealers or as funding portals, are required to make and preserve books and records.

While these costs will constitute part of the cost of compliance for entities that choose to become intermediaries in crowdfunding transactions by registering as broker-dealers, the cost of broker-dealer compliance with recordkeeping requirements of Rules 17a-3 and 17a-4 is not by itself a result of the final rule. Entities solely intending to serve as intermediaries in crowdfunding transactions for which the cost of compliance with broker-dealer recordkeeping requirements is too high may elect to register as funding portals. Funding portals will be required to make and keep records related to their activities to facilitate transactions in reliance on Section 4(a)(6), which we estimate for the purposes of the PRA to result in an initial burden of 325 hours and an initial cost of $5,350 per funding portal. We estimate that ongoing recordkeeping burden and cost will be similar to the initial burden and cost.[1591] We also note that some commenters stated that the cost burden for a funding portal to maintain the proposed books and records would not be significant.[1592] We recognize that there may be a slight competitive advantage for funding portals over broker-dealers to the extent that the recordkeeping rule for funding portals is less burdensome for than the requirements applicable to broker-dealers. At the same time, we believe that the recordkeeping rule for funding portals is consistent with the narrow range of their permitted activities.

6. Insignificant Deviations

We are providing a safe harbor for issuers for certain insignificant deviations from a term, condition or requirement of Regulation Crowdfunding.[1593] This safe harbor will provide that insignificant deviations from a term, condition or requirement of Regulation Crowdfunding will

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1591 *See* Section IV.C.2.n.

1592 *See* CFIRA Letter 1; Joinvestor Letter.

1593 *See* Rule 502(a) of Regulation Crowdfunding.

not result in a loss of the exemption, so long as the issuer relying on the exemption can show that: (1) the failure to comply was insignificant with respect to the offering as a whole; (2) the issuer made a good faith and reasonable attempt to comply with all applicable terms, conditions and requirements of Regulation Crowdfunding; and (3) the issuer did not know of the failure to comply, where the failure to comply with a term, condition or requirement was the result of the failure of the intermediary to comply with the requirements of Section 4A(a) and the related rules, or such failure by the intermediary occurred solely in offerings other than the issuer's offering.

The safe harbor is expected to decrease the costs incurred by issuers compared to the alternative of not providing a safe harbor. In the absence of a safe harbor, issuers might be hesitant to participate in this new marketplace for fear of inadvertently violating an applicable regulatory requirement, thereby reducing the benefits of Regulation Crowdfunding on efficiency, competition and capital formation. We recognize that providing a safe harbor can impose costs on investors, intermediaries and regulators, compared with the alternative of not providing a safe harbor, to the extent that issuers lessen the vigor with which they develop and implement systems and controls to achieve compliance with the requirements of Regulation Crowdfunding, which may result in a decrease in investor protection. Accordingly, we have designed the conditions of the safe harbor – specifically, the issuer must show that the failure to comply was insignificant with respect to the offering as a whole; it made a good faith and reasonable attempt to comply; and it did not know of the failure or such failure occurred solely in offerings other than the issuer's offering – to lessen the potential impact on investor protection.

Several commenters suggested that the safe harbor for insignificant deviations should not apply with respect to state regulatory enforcement actions.[1594] Adopting such an alternative could have significantly undermined the utility of the Section 4(a)(6) exemption by subjecting issuers to loss of state law preemption[1595] and potential state enforcement action for insignificant deviations from Regulation Crowdfunding's requirements.

7. Relationship with State Law

Section 305 of the JOBS Act amended Securities Act Section 18(b)(4)[1596] to preempt the ability of states to regulate certain aspects of crowdfunding conducted pursuant to Section 4(a)(6). This statutory amendment will benefit issuers by preempting any registration requirements in states in which they offer or sell securities in reliance on Section 4(a)(6), thereby reducing the costs for these transactions. It also can benefit investors because these cost savings ultimately may be passed on to investors. Absent preemption of state registration requirements, an offering made through the Internet in reliance on Section 4(a)(6) and the final rules could result in an issuer potentially violating state securities laws. Some evidence in donation-based and reward-based crowdfunding campaigns suggests that contributions are not exclusively local.[1597] The statutory preemption of state registration requirements will reduce issuer uncertainty about the necessity of state registration. On the other hand, state registration requirements may provide an additional layer of investor protection, and their preemption will remove a potential layer of

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1594 *See, e.g.*, Commonwealth of Massachusetts Letter; NASAA Letter.

1595 *See* Section III.B.7.

1596 15 U.S.C. 77r(b)(4).

1597 For example, in crowdfunding campaigns for early stage musical projects, the average distance between artist-entrepreneurs and contributors was 3,000 miles. *See* Ajay Agrawal, Christian Catalini and Avi Goldfarb, *The Geography of Crowdfunding*, NET Institute Working Paper No. 10-08 (Oct. 29, 2010), *available at* http://ssrn.com/abstract=1692661.

review that may help to deter fraud. This potential cost of state law preemption, however, may be offset by some of the statutory and final rule requirements that are designed to protect investors, such as public disclosure,[1598] investment limits,[1599] the use of a registered intermediary,[1600] provisions regarding measures to reduce the risk of fraud,[1601] and disqualification provisions.[1602] The requirement in the final rules that issuers file information on EDGAR also helps to ensure that information about issuers is available to individual state regulators, which retain the authority to bring enforcement actions for fraud.

8. Exemption from Section 12(g)

Rule 12g-6 provides that securities issued pursuant to an offering made under Section 4(a)(6) are exempted from the record holder count under Section 12(g) provided the issuer is current in its ongoing annual reports required pursuant to Rule 202 of Regulation Crowdfunding, has total assets as of the end of its last fiscal year not in excess of $25 million, and has engaged the services of a transfer agent registered with the Commission pursuant to Section 17A of the Exchange Act. The issuer size test is broadly consistent with some commenters' suggestions.[1603]

An issuer that exceeds the $25 million total asset threshold in addition to exceeding the thresholds in Section 12(g) will be granted a two-year transition period before it is required to register its class of securities pursuant to Section 12(g), provided it timely files all its ongoing reports due pursuant to Rule 202 of Regulation Crowdfunding during such period.[1604] Section

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1598 *See* Rule 201 of Regulation Crowdfunding.

1599 *See* Rule 100(a)(2) of Regulation Crowdfunding.

1600 *See* Rule 100(a)(3) of Regulation Crowdfunding.

1601 *See* Rule 301 of Regulation Crowdfunding.

1602 *See* Rule 503 of Regulation Crowdfunding.

1603 *See, e.g.*, ABA Letter ($25 million); PeoplePowerFund Letter.

1604 *Id.*

12(g) registration will be required only if, on the last day of the fiscal year in which the company exceeded the $25 million total asset threshold, the company has total assets of more than $10 million and the class of equity securities is held by more than 2,000 persons or 500 persons who are not accredited investors.[1605] In such circumstances, an issuer that exceeds the thresholds in Section 12(g) and has total assets of $25 million or more is required to begin reporting under the Exchange Act the fiscal year immediately following the end of the two-year transition period.[1606] An issuer entering Exchange Act reporting will be considered an "emerging growth company" to the extent the issuer otherwise qualifies for such status.

The conditional 12(g) exemption will defer the more extensive Exchange Act reporting requirements until the issuer either sells securities in a registered transaction or registers a class of securities under the Exchange Act. Consequently, smaller issuers will not be required to become an Exchange Act reporting company as a result of a Section 4(a)(6) offering. These offerings may have a large number of investors due to the limits on the amount each investor may invest and the absence of investor eligibility restrictions, or as a result of secondary market transactions in crowdfunding securities after the expiration of resale restrictions. Given the $1 million offering limitation, the potential cost of becoming an Exchange Act reporting company could have made many offerings in reliance on Section 4(a)(6) prohibitively costly.

The condition that the issuer remain current in its ongoing reporting, as suggested by one commenter,[1607] is intended to provide sufficient disclosure to help investors make informed decisions. We believe that the ongoing disclosures required of crowdfunding issuers in the final

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1605 15 U.S.C. 78*l*(g).

1606 17 CFR 240.12g-6.

1607 *See* Joinvestor Letter.

rules accomplish this objective and provide an appropriate consideration of investor protection and capital formation. This condition is expected to increase the level of investor protection by strengthening the incentives of securities-based crowdfunding issuers that exceed the Section 12(g) thresholds related to issuer size and the number of shareholders of record to comply with the ongoing reporting requirements of Regulation Crowdfunding. The extent of additional investor protection benefits from this condition is difficult to estimate, given a separate provision in the final rules that conditions the use of the Section 4(a)(6) exemption for future offerings on compliance with Regulation Crowdfunding's ongoing reporting requirements.

The issuer size limit condition is designed to be broadly consistent with the crowdfunding exemption being tailored to facilitate small company capital formation and the likely small size of a typical issuer in the crowdfunding market. This condition is expected to strengthen investor protection by reducing the likelihood that an issuer will grow and accumulate a significant number of investors as a result of multiple offerings in reliance on Section 4(a)(6) while remaining permanently exempt from the more extensive reporting requirements of the Exchange Act that would otherwise be required pursuant to Section 12(g) (unless the issuer registers a class of securities). The size limit condition will require larger issuers to provide investors with the more extensive disclosures required by the Exchange Act for reporting companies. However, we recognize that this condition also may subject crowdfunding issuers that are larger than the size threshold or that have a higher rate of growth, and are thus more likely to exceed the size threshold in the future, to the costs of Section 12(g) registration and Exchange Act reporting, potentially placing them at a competitive disadvantage to issuers that are close to but below the size threshold. It may also discourage some high-growth issuers from relying on Section 4(a)(6)

or may lead issuers approaching the size threshold to divest assets to remain under the threshold, potentially resulting in inefficient investment decisions.

While the condition requiring an issuer to use a registered transfer agent to rely on the exemption will impose costs on issuers,[1608] it is designed to provide investor protection benefits by introducing a regulated entity with experience in maintaining accurate shareholder records, thus helping to ensure that security holder records and secondary trades will be handled accurately.

9. Disqualification

The statute and the final rules impose disqualification provisions under which an issuer is not eligible to offer securities pursuant to Section 4(a)(6) and an intermediary is not eligible to effect or participate in transactions pursuant to Section 4(a)(6).[1609] The disqualification provisions for issuers are substantially similar to those imposed under Rule 262 of Regulation A and Rule 506 of Regulation D,[1610] while the disqualification provisions for intermediaries under Section 3(a)(39), which is an established standard for broker-dealers, are substantially similar to the provisions of Rule 262.

1608 *See* STA Letter (stating that strong competition in the registered transfer agent industry may result in monthly fees of $75 - $300 for transfer agent services, depending on a number of factors). *See also* CapSchedule Letter (stating that there exist cost-effective ways to keep records of security holders, such as "Software-As-A-Service" products, that costs $0 to set up initial records regardless of the number of investors, then pricing from $5 per month for up to 100 investors, $15 per month up to 1,000 investors and $25 per month for over 1,000 investors).

1609 *See* Section 302(d) of the JOBS Act and Rule 503 of Regulation Crowdfunding. *See also* discussion in Section II.E.6 above.

1610 *See Disqualification Adopting Release*, note 1182. *See also Regulation A Adopting Release*, note 506.

a. Issuers

The final rules are expected to induce issuers to implement measures to restrict bad actor participation in offerings made in reliance on Section 4(a)(6). This will help reduce the potential for fraud in the market for such offerings, which in turn may reduce the cost of raising capital to issuers that rely on Section 4(a)(6), to the extent that disqualification standards lower the risk premium associated with the presence of bad actors in securities offerings. In addition, the requirement that issuers determine whether any covered persons are subject to disqualification may obviate the need for investors to do their own investigations and eliminate redundancies that may exist in otherwise separate investigations. This is expected to help reduce information-gathering costs to investors, to the extent that issuers are at an advantage in accessing much of the relevant information and to the extent that issuers can do so at a lower cost than investors.

The final rules will, however, impose costs on some issuers, other covered persons and investors. If issuers are disqualified from relying on Section 4(a)(6) to make their offerings, they may experience increased costs in raising capital through alternative methods that do not require bad actor disqualification, if available, or they may be precluded from raising capital altogether. This can result in negative effects on capital formation. In addition, issuers may incur costs in connection with internal personnel changes that issuers may make to avoid the participation of those covered persons who are subject to disqualifying events. Issuers also may incur costs associated with restructuring share ownership positions to avoid having 20 Percent Beneficial Owners who are subject to disqualifying events. Finally, issuers may incur costs in connection with seeking waivers of disqualification from the Commission or determinations by other authorities that existing orders do not give rise to disqualification.

The final rules provide a reasonable care exception whereby an issuer will not lose the benefit of the Section 4(a)(6) exemption if it is able to show that it did not know, and in the exercise of reasonable care could not have known, of the existence of a disqualification.[1611] A reasonable care exception may encourage capital formation by eliminating any hesitation issuers may otherwise experience under a strict liability standard. However, such an exception also may encourage issuers to take fewer steps to inquire about the existence of a disqualification than they would if a strict liability standard applied, increasing the potential for fraud in the market for offerings made in reliance on Section 4(a)(6). Nevertheless, some issuers, in exercising reasonable care, may incur costs associated with conducting and documenting their factual inquiry into possible disqualifications. The lack of specificity in the rule, while providing flexibility to the issuer to tailor its factual inquiry as appropriate to a particular offering, may increase these costs because uncertainty can drive issuers to do more than necessary under the rule.

The requirement under the final rules that issuers disclose matters that would have triggered disqualification, had they occurred after the effective date of Regulation Crowdfunding,[1612] also will impose costs and benefits. The disclosure requirement will reduce costs associated with covered persons who would be disqualified under the final rules but for the fact that the disqualifying event occurred prior to the effective date of the rules. However, this approach will allow the participation of past bad actors, whose disqualifying events occurred prior to the effective date of the final rules, which can expose investors to the risks that arise when bad actors are associated with an offering. Nevertheless, investors will benefit by having access to such information that can inform their investment decisions. Issuers also may incur costs

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[1611] *See* Rule 503(b)(4) of Regulation Crowdfunding. *See also* Section II.E.6.a.iii.

[1612] *See* Rule 201(u) of Regulation Crowdfunding. *See also* Section II.E.6.a.v.

associated with the factual inquiry, preparing the required disclosure and making any internal or share ownership changes to avoid the participation of covered persons that trigger the disclosure requirement. Disclosure of triggering events also may make it more difficult for issuers to attract investors, and issuers may experience some or all of the impact of disqualification as a result.

We believe the inclusion of Commission cease-and-desist orders in the list of disqualifying events will not impose a significant, incremental cost on issuers and other covered persons because many of these actors may already be subject to disqualifying orders issued by the states, federal banking regulators and the National Credit Union Administration.[1613]

Under the final rules, orders issued by the CFTC will trigger disqualification to the same extent as orders of the regulators enumerated in Section 302(d)(2)(B)(i) of the JOBS Act (*e.g.*, state securities, insurance and banking regulators, federal banking agencies and the National Credit Union Administration). We believe that including orders of the CFTC will result in the similar treatment, for disqualification purposes, of comparable sanctions. In this regard, we note that the conduct that will typically give rise to CFTC sanctions is similar to the type of conduct that will result in disqualification if it were the subject of sanctions by another financial services industry regulator. This is likely to enable the disqualification rules to more effectively screen out bad actors.

As discussed above, the baseline for our economic analysis of Regulation Crowdfunding, including the baseline for our consideration of the effects of the final rules on efficiency, competition and capital formation, is the situation in existence today, in which startups and small businesses seeking to raise capital through securities offerings must register the offer and sale of securities under the Securities Act unless they can comply with an existing exemption from

[1613] *See Disqualification Adopting Release*, note 1182.

registration under the federal securities laws. Relative to the current baseline, we believe that the disqualification provisions will not impose significant incremental costs on issuers and other covered persons because the final rules are substantially similar to the disqualification provisions under existing exemptions.

As an alternative, we could have specified that pre-existing events are subject to the disqualification rules, as suggested by some commenters.[1614] As another alternative, we could have expanded the list of covered persons to include transfer agents and lawyers, as suggested by one commenter.[1615] By expanding the range and categories of potentially disqualified persons, both of these alternatives could have the benefit of strengthening investor protection. At the same time, they would increase the compliance costs for issuers and disqualified persons described above. Overall, we believe that preserving consistency with the disqualification criteria of Rule 262 and Rule 506, as we do in the final rules, can potentially yield compliance cost savings for issuers that undertake multiple types of exempt offerings while still maintaining appropriate investor protections.

b. Intermediaries

With regard to intermediaries, the final rules apply the disqualification provisions under Section 3(a)(39) of the Exchange Act, rather than a standard based on Rule 262.[1616] The Section 3(a)(39) standard is an established one among broker-dealers and their regulators, and we believe that, despite the differences, Section 3(a)(39) and Rule 262 are substantially similar with regard to

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1614 *See, e.g.,* Guzik Letter 1; NASAA Letter.

1615 *See* Brown J. Letter (also recommending the Commission adopt similar bad actor provisions under Rule 504).

1616 *See* Rule 503(d) of Regulation Crowdfunding.

the persons and events they cover, their scope and their purpose.[1617] We believe that imposing any new or different standard, including one based on Rule 262, for those intermediaries that engage in crowdfunding transactions would likely create confusion and unnecessary burdens, as currently-registered broker-dealers and their associated persons would become subject to two distinct standards for disqualification. Moreover, adopting a more stringent disqualification standard may reduce the number of intermediaries eligible under the final rules and decrease competition among intermediaries in the securities-based crowdfunding market. By contrast, consistent standards for all broker-dealers and funding portals will assist a registered national securities association in monitoring compliance and enforcing its rules.

The final rules implement the statutory requirement for intermediaries by providing that a person subject to a statutory disqualification, as defined in Exchange Act Section 3(a)(39), may not act as, or be an associated person of, an intermediary in a transaction involving the offer or sale of securities in reliance on Section 4(a)(6) unless so permitted by Commission rule or order. While this requirement will potentially reduce the number of intermediaries for Section 4(a)(6) transactions, we expect that it will strengthen investor protection by preventing bad actors from entering the securities-based crowdfunding market, thereby reducing the potential for fraud and other abuse.

As discussed above, the baseline for our economic analysis of Regulation Crowdfunding, including the baseline for our consideration of the effects of the final rules on efficiency, competition and capital formation, is the situation in existence today, in which intermediaries intending to facilitate securities transactions are required to register with the Commission as broker-dealers under Exchange Act Section 15(a). Relative to this baseline, we believe that the

[1617] *See* discussion in Section II.E.6.b above.

disqualification provisions will not impose significant incremental costs to broker-dealers because the final rules include the same disqualification provisions that are already imposed on broker-dealers.

IV. PAPERWORK REDUCTION ACT

A. Background

Certain provisions of the final rules contain "collection of information" requirements within the meaning of the Paperwork Reduction Act of 1995 ("PRA").[1618] We published a notice requesting comment on the collection of information requirements in the Proposing Release, and we submitted the proposal to the Office of Management and Budget ("OMB") for review in accordance with the PRA.[1619]

In the Proposing Release, we solicited comment on the assumptions and estimates in our PRA analysis. We received no comments on our estimates of and assumptions about the number of issuers and intermediaries that will participate in securities-based crowdfunding transactions or the size and frequency of those transactions. We received several comments on our estimates of the time and expense required of issuers to meet their filing obligations.[1620] We also received several comments on our estimates of the costs incurred by intermediaries.[1621] One commenter recommended a lessened paperwork burden in general.[1622] These comments are discussed in further detail below, and where appropriate, we have revised our burden estimates in response to commenters' suggestions and to reflect changes in the final rules, as adopted.

1618 44 U.S.C. 3501 *et seq.*

1619 44 U.S.C. 3507(d); 5 CFR 1320.11.

1620 *See, e.g.,* Angel Letter 1; Heritage Letter; SeedInvest Letter 1.

1621 *See, e.g.,* Arctic Island Letter 8; CapSchedule Letter; Heritage Letter; Joinvestor Letter; SBEC Letter; Seed & Spark Letter; STA Letter.

1622 Peers Letter.

The titles for the collections of information are:

(1) "Form ID" (OMB Control Number 3235-0328);

(2) "Form C" (OMB Control Number 3235-0716) (a new collection of information);

(3) "Form BD" (OMB Control Number 3235-0012); and

(4) "Crowdfunding Rules 300-304 – Intermediaries" (OMB Control Number 3235-0726)[1623] (a new collection of information) and

(5) "Crowdfunding Rules 400-404 – Funding Portals" (OMB Control Number 3235-0727)[1624] (a new collection of information).

An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless it displays a currently valid OMB control number. We applied for OMB control numbers for the new collections of information in accordance with 44 U.S.C. 3507(j) and 5 CFR 1320.13, and as of the date of this release, OMB has assigned a control number to each new collection as specified above. Responses to these new collections of information will be mandatory for issuers raising capital under Regulation Crowdfunding and intermediaries participating in offerings under Regulation Crowdfunding.

The hours and costs associated with preparing disclosure, filing forms, and retaining records constitute reporting and cost burdens imposed by the collections of information. In deriving estimates of these hours and costs, we recognize that the burdens likely will vary among individual issuers and intermediaries based on a number of factors, including the stage of development of the business, the amount of capital an issuer seeks to raise, the number of

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[1623] This includes burdens for compliance with privacy rules (Reg. S-P, Reg. S-AM and Reg S-ID) as required by Rule 403(b).

[1624] This includes burdens for Form Funding Portal.

offerings an intermediary hosts on its platform, and the number of years since inception of the business. We believe that some issuers and intermediaries will experience costs in excess of the average and some issuers and intermediaries may experience less than the average costs.

B. Estimate of Issuers and Intermediaries

1. Issuers

The number, type and size of the issuers that will participate in securities-based crowdfunding transactions are uncertain, but data on current market practices may help identify the number and characteristics of potential issuers that may offer and sell securities in reliance on Section 4(a)(6).[1625] While it is not possible to predict the number of future offerings made in reliance on Section 4(a)(6), particularly because rules governing securities-based crowdfunding are not yet in effect, for purposes of this analysis, we estimate that approximately 1,900 issuers will seek to offer and sell securities in reliance on Section 4(a)(6) per year. We base this estimate on the average number of issuers (excluding issuers that are pooled investment vehicles) per year that conducted a new Regulation D offering of up to $1 million from 2009 to 2014 and had no revenues or less than $1 million in revenues.[1626] We believe those issuers will be similar in size to the potential issuers that may participate in securities-based crowdfunding, and we assume that each issuer will conduct one offering per year.

We received no comments on our estimate of the number of issuers expected to participate in securities-based crowdfunding transactions or the number of offerings in reliance on Section

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1625 *See* Section III.A.5.a for a discussion of the data regarding current market practices.

1626 *Id.* This estimate differs from our estimate in the proposal. It uses more recent data than the proposal and is based on the average number of issuers per year rather than the average number of unique issuers. According to filings made with the Commission, an average of approximately 4,559 issuers per year conducted new Regulation D offerings of up to $1 million from 2009 to 2014. 22%, or 1,003, of those issuers reported having no revenues. (0.22 x 4,559 = 1,003). 19%, or 866, of those issuers reported having less than $1 million in revenues. (0.19 x 4,559 = 866). Therefore, the average number of issuers per year is 1,003 + 866 = 1,869, or approximately 1,900 issuers.

4(a)(6) we expect those issuers to conduct. In developing the estimate for the number of issuers in the final rule, we refined the methodology used in the Proposing Release and applied that methodology to more recent data, resulting in an updated estimate that we believe is reasonable and appropriate.

2. Intermediaries that are Registered Brokers

The final rules require intermediaries to register with us as either a broker-dealer or as a funding portal. Consistent with the Proposing Release, we estimate that the collection of information requirements in the final rules will apply to approximately 10 intermediaries per year that are not currently registered with the Commission and that will choose to register as brokers, rather than as funding portals, to act as intermediaries for offerings made in reliance on Section 4(a)(6). However, we believe that, given the cost that an unregistered entity will incur to register as a broker compared with the lower cost of becoming a funding portal, unregistered entities that choose to act as crowdfunding intermediaries will generally be more likely to register as funding portals than as brokers.

Consistent with the Proposing Release, we further estimate that approximately 50 intermediaries per year that are already registered as brokers with the Commission will choose to add to their current service offerings by also serving as crowdfunding intermediaries. These entities will not have to file a new application for registration with us, and if currently doing business with the public, they will already be members of FINRA (the applicable national securities association registered under Exchange Act Section 15A). We note, however, that given the nascent nature of the equity-based crowdfunding market, we do not have any data or other evidence indicating the number of currently-registered brokers that will be interested in becoming crowdfunding intermediaries. Therefore, we recognize that the number of brokers per year that

may engage in crowdfunding activities could differ significantly from our current estimate. We received no comments on our estimates of the number of broker-dealers that will act as intermediaries.

3. Funding Portals

Consistent with the Proposing Release, we estimate that on average approximately 50 intermediaries per year that are *not* already registered as brokers will choose to be registered as funding portals during the first three years following effectiveness of the final rules. This estimate assumes that, upon effectiveness of the final rules, about 15% of the approximately 200 U.S.-based crowdfunding portals[1627] currently in existence will participate in securities-based crowdfunding and that the number of crowdfunding portals will grow at 60% per year over the next three years.[1628] Therefore, we estimate that an average of approximately 50 respondents will be registered as funding portals annually.[1629] Of those 50 funding portals, we estimate that two will be nonresident funding portals. These estimates are based in part on indications of interest

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1627 This estimate is based in part on an industry estimate that, as of April 2012, there were approximately 200 non-securities-based crowdfunding portals operating in the United States. *See* Massolution 2012 at 16. We did not receive comment on these estimates and therefore continue to believe our estimates in the Proposing Release are appropriate. *See also* Massolution 2015 at 84 (estimating that, as of December 2014, there were approximately 375 crowdfunding portals operating in North America, not just the United States).

1628 A worldwide survey of crowdfunding portals indicated that, in 2011, approximately 14.8% of the surveyed crowdfunding portals (mostly based in Europe) participated in "equity-based" crowdfunding. *Id*. Also, the total number of crowdfunding portals worldwide grew by an estimated 60% from 2011 to 2012. *Id*. at 13. We did not receive comment on these estimates and therefore continue to believe our estimates in the Proposing Release are appropriate. *See also* Massolution 2015 at 82-83 (estimating that, as of December 2014, there were approximately 1250 crowdfunding portals worldwide compared to 813 worldwide in 2012, which represents an increase of approximately 54%).

1629 200 U.S.-based crowdfunding portals x 15% (estimated percentage of crowdfunding portals that will participate in securities-based crowdfunding) = 30 funding portals that will participate in securities-based crowdfunding. Assuming 60% growth over three years, the number of registered funding portals will be 30 during the first year, 48 during the second year and 77 during the third year. The average number of registered funding portals over three years is (30 + 48 + 77) / 3 = 52 funding portals (or approximately 50 funding portals per year).

expressed in responses to FINRA's voluntary interim form for funding portals. We received no comments on our estimates on the number of funding portals that will act as intermediaries

C. Estimate of Burdens

1. Issuers

a. Form C: Offering Statement and Progress Update

Under the final rules, an issuer conducting a transaction in reliance on Section 4(a)(6) will be required to file with us specified disclosures on a Form C: Offering Statement.[1630] An issuer also will be required to file with us amendments to Form C to disclose any material change in the offer terms or disclosure previously provided to investors.[1631] Form C is similar to the Form 1-A offering statement under Regulation A, but it requires fewer disclosure items (*e.g.*, it does not require disclosure about the plan of distribution, the compensation of officers and directors, litigation or a discussion of federal tax aspects). We note that offerings made in reliance on Regulation A allow issuers to offer up to $50 million, involve review by SEC staff and, in the case of Tier 1 offerings, require filings at the state level.[1632] In light of these factors, we expect that issuers seeking to raise capital pursuant to a Regulation A offering generally will be at a more advanced stage of development than issuers likely to raise capital pursuant to Section 4(a)(6), so the complexity of the required disclosure and, in turn, the burden of compliance with the requirements of Form C will be significantly less than for Form 1-A.[1633] In the Proposing Release we estimated that the burden to prepare and file Form C would be approximately 60 hours per

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1630 *See* Rule 203(a)(1) of Regulation Crowdfunding.

1631 *See* Rule 203(a)(2) of Regulation Crowdfunding.

1632 *See* Rule 256 of Regulation A; *Regulation A Adopting Release*, note 506.

1633 We currently estimate the average burden per response for preparing and filing a Form 1-A to be approximately 750 hours.

issuer, which represented approximately 10% of the burden to prepare then-existing Form 1-A.[1634] We estimated that 75% of the burden, or 45 hours, would be carried internally and the remaining 25% of the burden would be carried by outside professionals at a cost of $6,000 per issuer.

As discussed in more detail in the Economic Analysis, above, we received a number of comments concerning the burdens and costs of the proposed rules.[1635] Many of these commenters provided monetary estimates without distinguishing between internal burden hours and outside professional costs. Some commenters suggested that the Proposing Release underestimated the time and expense that would be required to prepare and file Form C.[1636] In contrast, one commenter stated that it was a third-party service provider that could prepare Form C at much lower costs than those estimated by the Commission.[1637] Another commenter suggested that the cost of preparing and filing these forms and the associated compliance costs would range from $3,000 to $9,000.[1638] Additionally, we received a number of comments about the costs of the audit and review of financial statements, as proposed. We believe that these costs would be a component of the outside professional costs associated with Form C. In the Economic Analysis, we have set forth our monetized estimates of the various cost components, grouped into categories

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1634 *See* Proposing Release at 78 FR 66540.

1635 *See* Section III.B.3.a.

1636 *See, e.g.,* Heritage Letter (stating that the costs to prepare the required disclosures will likely exceed $10,500, except in cases of start-ups with no operating history); NSBA Letter (stating that issuers and intermediaries will likely incur higher attorney and accounting fees and financial and administrative burdens than estimated in the proposed rules but without providing estimates); SeedInvest Letter 2 (estimating upfront compliance costs to be "potentially hundreds of hours [in internal company time] and $20,000 to $50,000 [in outside professional costs]").

1637 FundHub Letter 2 (stating that the commenter will prepare Form C and all disclosure documents, do all bad actor checks, verify investor status and perform all other necessary compliance measures for a $100,000 offering for $2,500 total, and that, in most cases, its services and associated legal fees will cost an issuer between $2,500 and $5,000 for an offering up to $500,000 and between $5,000 and $10,000 for an offering between $500,000 and $1,000,000).

1638 *See* StartEngine Letter 2.

based on the size of the offering. Our Form C estimates range from $2,500 for the smallest offerings (up to $100,000); to a range of $2,500 to $5,000 for somewhat larger offerings (more than $100,000 but not more than $500,000) and a range of $5,000 and $20,000 for the largest offerings (more than $500,000). Additionally, our estimates of the cost of financial statement review or audit range from $0 for the smallest offerings; to between $1,500 and $18,000 for larger offerings and for first-time crowdfunding issuers conducting offerings between $500,000 and $1,000,000; and $2,500 to $30,000 for other issuers that are conducting an offering in the largest offering amount category. Accordingly, in our Economic Analysis we estimate a cost range estimate for Form C and the financial statement review of: $2,500 for the smallest offerings, $4,000 to $23,000 for the larger offerings, $6,500 to $38,000 for first-time crowdfunding issuers conducting offerings between $500,000 and $1,000,000, and $7,500 to $50,000 for other issuers conducting an offering in the largest offering amount category. For purposes of the PRA, however, we must provide a single estimate, comprised of both burden hours and outside professional costs, for an average issuer.

Based on these comments and our Economic Analysis, we have revised our estimate of the burden associated with the preparation and filing of Form C. We acknowledge that a number of commenters suggested that we underestimated the burdens of the proposed rule, but believe that changes in the final rule, particularly with respect to the financial statement requirements for first-time crowdfunding issuers, may mitigate the impact of those costs. Accordingly, we estimate that the average total burden to prepare and file the Form C, including any amendment to disclose any material change, will be approximately 100 hours, which, while higher than our proposed estimate, is still substantially less than the burden to prepare a Form 1-A for an offering under Regulation A, as recently amended. We continue to estimate that 75 percent of the burden of

preparation will be carried by the issuer internally and that 25 percent will be carried by outside professionals[1639] retained by the issuer at an average cost of $400 per hour.[1640] This reflects 75 internal burden hours per issuer and $10,000 in external professional costs. While for PRA purposes, we must present this estimate in terms of hours and costs, we believe that this estimate is consistent with the monetary ranges that we set forth in the Economic Analysis.

Under the final rules, the issuer also will be required to file with us regular updates on the progress of the issuer in meeting the target offering amount.[1641] In a change from the proposal, the rules permit issuers to satisfy the progress update requirement by relying on the relevant intermediary to make publicly available on the intermediary's platform frequent updates about the issuer's progress toward meeting the target offering amount. Nevertheless, an issuer relying on the intermediary's reports of progress must still file a progress update at the end of the offering to disclose the total amount of securities sold in the offering. The issuer is required to make the filing under cover of a Form C-U: Progress Update. Form C-U is similar to a Form D Notice of Exempt Offering of Securities under Regulation D.[1642] Form C-U will require significantly less disclosure than the Form D, however, as it will require disclosure only of the issuer's progress in meeting the target offering amount, rather than compensation and use of proceeds disclosures or other information about the issuer and the offering. Thus, the complexity of the required

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1639 For example, an issuer could retain an outside professional to assist in the preparation of the financial statements, but could decide to address the remaining disclosure requirements internally.

1640 We estimate the average external cost of preparing Form C to be 0.25 x 100 hours x $400 per hour = $10,000.

We recognize that the costs of retaining outside professionals may vary depending on the nature of the professional services, but for purposes of this PRA analysis, we estimate that such costs would be an average of $400 per hour. This is the rate we typically estimate for outside legal services used in connection with public company reporting.

1641 *See* Rule 203(a)(3) of Regulation Crowdfunding.

1642 We currently estimate the burden per response for preparing and filing a Form D to be 4.00 hours.

disclosure and the burden to prepare and file Form C-U will be significantly less than for Form D. We continue to estimate that the burden to prepare and file each progress update will be 0.50 hours. In light of the change from the proposal, we expect most issuers will rely on the relevant intermediary to provide interim progress updates and therefore will be required to file an average of one progress update during each offering rather than the two progress updates that we estimated in the Proposing Release.[1643] As in the Proposing Release, we estimate that the entirety of this burden will be borne internally by the registrant.

Overall, we estimate that compliance with the requirements of a Form C filed in connection with offerings made in reliance on Section 4(a)(6) will require 190,000 burden hours (1,900 offering statements x 100 hours/offering statement) in aggregate each year, which corresponds to 142,500 hours carried by the issuer internally (1,900 offering statements x 100 hours/offering statement x 0.75) and costs of $19,000,000 (1,900 offering statements x 100 hours/offering statement x 0.25 x $400) for the services of outside professionals. We also estimate that compliance with the requirements of Form C-U filed during an offering will require 950 burden hours (1,900 offering statements x 1 progress update per offering x 0.50 hours per progress update) in aggregate each year.

b. Form C-AR: Annual Report

Under the final rules, unless the reporting has been terminated, any issuer that sells securities in a transaction made pursuant to Section 4(a)(6) will be required to file annually with us an annual report on Form C-AR: Annual Report.[1644] Form C-AR will require disclosure substantially similar to the disclosure provided in the Form C: Offering Statement, except that

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1643 *See* Rule 203(a)(3) of Regulation Crowdfunding.

1644 *See* Rule 202 of Regulation Crowdfunding.

offering-specific disclosure will not be required and the issuer may be able to update disclosure previously provided in the Form C. In addition, in a change from the proposal, instead of requiring financial statements in the annual report that meet the highest standard of review previously provided (either reviewed or audited), the final rules require financial statements of the issuer certified by the principal executive officer of the issuer to be true and complete in all material respects.[1645] Therefore, we estimate that the burden to prepare and file Form C-AR will be less than that required to prepare and file Form C.

As discussed in the Economic Analysis, we received some comments on the costs of Form C-AR.[1646] One commenter that submitted comments concerning both Form C and Form C-AR provided several cost estimates or ranges for Form C-AR that varied but were ranges or amounts that were lower than the commenter's estimates for Form C.[1647] Our analysis of the cost of Form C-AR in our Economic Analysis reflects these comments, and in that analysis, we estimate that the cost of Form C-AR represents two-thirds of the cost of Form C (exclusive of the financial statement review).

Additionally, in light of the change to the final rules for Form C-AR to require financial statements that are certified by the principal executive officer of the issuer to be true and complete in all material respects, rather than requiring financial statements that meet the highest level of review previously provided, we estimate that for Form C-AR there will be a further reduction of PRA burden compared with the burden of Form C. Accordingly, we estimate that compliance

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1645 *See* Rule 202(a) of Regulation Crowdfunding. However, issuers that have available financial statements that have been reviewed or audited by an independent certified public accountant because they prepare them for other purposes shall provide them and will not be required to have the principal executive officer certification. *Id.*

1646 *See* Section III.B.3.a.

1647 *See* SeedInvest Letter 1; SeedInvest Letter 4

with Form C-AR will be approximately one-half of the burden of Form C, resulting in a burden of 50 hours per response. We further estimate that 75 percent of the burden of preparation will be carried by the issuer internally and that 25 percent will be carried by outside professionals[1648] retained by the issuer at an average cost of $400 per hour.[1649]

We estimate that compliance with the requirements of Form C-AR in the first year after issuers sell securities pursuant to Section 4(a)(6) will require 95,000 burden hours (1,900 issuers x 50 hours/issuer) in the aggregate, which corresponds to 71,250 hours carried by the issuer internally (1,900 issuers x 50 hours/issuer x 0.75) and costs of $9,500,000 (1,900 issuers x 50 hours/issuer x 0.25 x $400) for the services of outside professionals.

c. Form C-TR: Termination of Reporting

Under the final rules, any issuer terminating its annual reporting obligations will be required to file a notice under cover of Form C-TR: Termination of Reporting to notify investors and the Commission that it no longer will file and provide annual reports pursuant to the requirements of Regulation Crowdfunding.[1650] We estimate that eight percent of the issuers that sell securities pursuant to Section 4(a)(6) will file a notice under cover of Form C-TR during the first year.[1651] The Form C-TR will be similar to the Form 15 that issuers file to provide notice of termination of the registration of a class of securities under Exchange Act Section 12(g) or to provide notice of the suspension of the duty to file reports required by Exchange Act Sections

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1648 *See* note 1639.

1649 *See* note 1640.

1650 *See* Rule 203(b)(2) of Regulation Crowdfunding.

1651 For purposes of this PRA analysis, we estimate that eight percent of issuers will not survive past their first year, based on a recent study that found that of a random sample of 4,022 new high-technology businesses started in 2004, 92.3% survived past their first year. *See* Kauffman Firm Survey, note 1302 at 13.

13(a) or 15(d).[1652] Therefore, we estimate that compliance with the Form C-TR will result in a similar burden as compliance with Form 15, that is, a burden of 1.50 hours per response. We estimate that compliance with Form C-TR will result in a burden of 228 hours (1,900 issuers x 0.08 issuers filing Form C-TR x 1.50 hours/issuer) in the aggregate during the first year for issuers terminating their reporting obligations. As in the Proposing Release, we estimate that the entirety of this burden will be borne internally by the registrant. We received no comments on our estimates with respect to Form C-TR and continue to believe that these estimates are reasonable.

d. Form ID Filings

Under the final rules, an issuer will be required to file specified disclosures with us on EDGAR.[1653] We anticipate that the majority of first-time issuers seeking to offer and sell securities in reliance on Section 4(a)(6) will not previously have filed an electronic submission with us and so will need to file a Form ID. Form ID is the application form for access codes to permit filing on EDGAR. The final rules will not change the form itself, but we anticipate that the number of Form ID filings will increase due to new issuers seeking to offer and sell securities in reliance on Section 4(a)(6). One commenter stated that it would take approximately 70 minutes to complete a Form ID, considerably more time than the estimated 0.15 hours.[1654] However, the information required by Form ID is very limited, primarily the name and address of the filer, so we continue to believe the estimated 0.15 hours per response is appropriate. For purposes of this PRA analysis, we estimate that all of the issuers who will seek to offer and sell securities in reliance on Section 4(a)(6) will not have filed an electronic submission with us previously and

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1652 We currently estimate the burden per response for preparing and filing a Form 15 to be 1.50 hours.

1653 *See* Rules 201-203 of Regulation Crowdfunding.

1654 Angel Letter 1.

will, therefore, be required to file a Form ID. As noted above, we estimate that approximately 1,900 issuers per year will seek to offer and sell securities in reliance on Section 4(a)(6), which will correspond to 1,900 additional Form ID filings. As a result, we estimate the additional annual burden associated with this form will be approximately 285 hours (1,900 filings x 0.15 hours/filing).[1655]

2. Brokers and Funding Portals

Below, we discuss our estimates of the internal burdens and professional costs associated with the collections of information required under the final rules as they relate to intermediaries. Where relevant, we discuss any comments received on these estimates and any changes to estimates, including changes made in response to comments on them.

a. Registration Requirements

(1) Time Burden

The final rules will require intermediaries to register with us as either a broker or as a funding portal. As noted above, we believe that some intermediaries for transactions made in reliance on Section 4(a)(6) and Regulation Crowdfunding will already be registered as brokers. Therefore, this registration requirement will impose no new requirement on these entities and no additional burden for purposes of this PRA analysis. Entities that are not already registered as brokers may decide to register either as brokers or as funding portals and to become members of a registered national securities association (if they are not already a member) pursuant to the final rules. We estimate that each year, on average, approximately 10 entities may decide to be registered as brokers and approximately 50 entities may decide to be registered as funding portals

[1655] We currently estimate the burden per response for preparing and filing with Form ID to be 0.15 hours.

by filing Form Funding Portal.[1656] In addition, we estimate that of those 50 entities that register as funding portals, two will be nonresident funding portals and subject to the additional requirements under Rule 400(f) of completing Schedule C (including the required certifications), requirements related to the agent for service of process in the United States, and obtaining an opinion of counsel.

We estimate the burden for registering with the Commission as a broker based upon the existing burdens for completing and filing Form BD, currently estimated as 2.75 hours.[1657] Consequently, we estimate that the total annual burden hours required for all crowdfunding intermediaries, including brokers and funding portals, to register with us under the final rules will be approximately 165 hours (2.75 hours/respondent x (10 brokers + 50 funding portals)). In addition, those entities that register as nonresident funding portals will face an additional burden of half an hour to complete Schedule C and make the required certifications, half an hour to document the appointment of an agent for the service of process, and one hour to obtain an opinion of counsel. Consequently, we estimate that, of the 50 registered funding portals, two will each face an additional burden of two hours to register, for a total additional annual burden of four hours.

We have taken into consideration that brokers that register to engage in crowdfunding transactions conducted in reliance on Section 4(a)(6) may eventually decide to withdraw their

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1656 As noted above, funding portals will have to complete and file Form ID in order to obtain access codes to file on EDGAR. Based on our estimates, 50 funding portals per year will newly register through EDGAR, which will correspond to 50 additional Form ID filings. As a result, we estimate the additional annual burden associated with this form will be approximately 7.5 hours (50 filings x 0.15 hours/filing).

1657 While it is likely that the time necessary to complete Form BD varies depending on the nature and complexity of the entity's securities business, we currently estimate the average time necessary for a broker-dealer to complete and file an application for broker-dealer registration on Form BD to be approximately 2.75 hours. We also estimate that the time burden to register as a funding portal on Form Funding Portal will be, for purposes of this PRA analysis, the same as the time required to complete and file Form BD because the information required for that form is similar.

registration. Withdrawal requires an entity to complete and file with us a Form BDW.[1658] We further estimate that approximately 430 broker-dealers withdraw from Commission registration annually[1659] and, therefore, file a Form BDW. Of them, we estimate that approximately one broker who had registered in order to facilitate crowdfunding offerings made in reliance on Section 4(a)(6) will decide to withdraw in each year following adoption of the rules.[1660] Therefore, the one broker-dealer that withdraws from registration by filing Form BDW will incur an aggregate annual reporting burden of approximately 0.25 hours (0.25 hours/respondent x 1 broker). Similarly, we estimate that approximately five funding portals will choose to withdraw from registration each year[1661] and that each withdrawal, as with Form BDW, will take approximately 0.25 hours. This will result in an aggregate annual reporting burden of approximately 1.25 hours (0.25 hours/respondent x 5 funding portals).

1658 The time necessary to complete Form BDW varies depending on the nature and complexity of the applicant's securities business. We currently estimate that it takes a broker-dealer approximately 0.25 burden hours to complete and file a Form BDW to withdraw from Commission registration, as required by Exchange Act Rule 15b6-1 (17 CFR 240.15b6-1).

1659 This estimate is based on Form BDW data collected over the past five years and may be high as a result of the impact of the financial crisis on broker-dealers. For the past five fiscal years (from 10/1 through 9/30), the number of broker-dealers that withdrew from registration was as follows: 524 in 2011 and 428 in 2012, 434 in 2013, 454 in 2014 and 306 by September 15, 2015. We thus estimate the number of broker-dealers that withdraw from the Commission annually to be 430 ((524+428+434+454+306) / 5).

1660 As of September 2015, there were 4,213 broker-dealers registered with the Commission. An average of 430 broker-dealers per year withdraw from registration, or 10% of the number of registered broker-dealers (430 withdrawing broker-dealers / 4,213 registered broker-dealers). We assume that the same percentage of broker-dealers that withdraw from registration will apply to the population of registered broker-dealers participating in offerings in reliance on Section 4(a)(6). Of our estimate of 10 registered broker-dealers per year registering to participate in crowdfunding transactions in reliance on Section 4(a)(6), we estimate that approximately one broker-dealer per year (10 registered broker-dealers x 0.10) will withdraw from registration.

1661 We estimate that the percentage of registered funding portals participating in crowdfunding transactions in reliance on Section 4(a)(6) that will withdraw from registration annually would be the same as the percentage of broker dealers that withdraw from registration annually because of the similarity of these entities' businesses. Of our estimate of 50 registered funding portals participating in crowdfunding transactions in reliance on Section 4(a)(6), we estimate that approximately five funding portals per year (50 registered funding portals x 0.10) will withdraw from registration. For funding portals, a decision to withdraw registration will be required to be reported to us in the same way as an amendment; however, for brokers, withdrawal requires the filing of Form BDW.

In the Proposing Release, we also included an estimate of PRA burdens and costs for newly-registered intermediaries to become members of FINRA or any other registered national securities association. Specifically, the Proposing Release included a discussion of an estimate of the paperwork burdens and costs that would be incurred by an intermediary to register with a national securities association as well as an estimate of the ongoing fees (e.g., FINRA annual assessment fees) that would be incurred by an intermediary to remain registered with a national securities association. However, after further consideration, we do not believe the hour burdens and costs associated with FINRA's membership constitute paperwork burdens and costs attributable to the Commission's rules. Accordingly, we are not providing estimates of burdens and costs resulting from membership in a registered national securities association in this PRA analysis. We have, however, considered the costs of such membership, both initial and ongoing, in our Economic Analysis above.[1662]

Once registered, a broker must promptly file an amended Form BD when information originally reported on Form BD changes or becomes inaccurate. Similarly, a registered funding portal must file amendments relating to changes in information filed in a Form Funding Portal filing.[1663] Based on the number of amended Forms BD that we received from October 1, 2011 through September 15, 2015, we estimate that the total number of amendments that we will receive on Form BD from the 10 brokers that register under Regulation Crowdfunding will be approximately 32.[1664] Therefore, we estimate that the total additional annual burden hours

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1662 *See* Section III.B.4.

1663 We currently estimate that the average time necessary to complete an amended Form BD to be approximately 20 minutes, or 0.33 hours. We estimate that an amendment to Form Funding Portal will take the same amount of time as an amendment to Form BD because the forms are similar.

1664 We received 15,491, 13,271, 12,902, 14,330 and 10,848 amended Forms BD during the fiscal years ending 2011, 2012, 2013, 2014 and 2015, respectively, reflecting an average of 13,368 amendment filings per year

necessary for broker-dealers to complete and file amended Forms BD will be approximately 10.6 hours (32 amended Forms BD per year x 0.33 hours). Using the same ratios, we estimate that the total annual burden hours for funding portals to complete and file amended Forms Funding Portal will be approximately 52.8 hours (50 funding portals x 3.2 amendments per year x 0.33 hours per amendment).

(2) Cost

We estimate that two intermediaries will face a cost per intermediary of $25,179 to retain an agent for service of process and provide an opinion of counsel to register as a nonresident funding portal.[1665]

b. Development of Intermediary Platform

(1) Time Burden

The final rules envision that intermediaries will develop electronic platforms to offer securities to the public in reliance on Section 4(a)(6). We anticipate that an intermediary's platform will incorporate related systems functionality to comply with our final rules (including the collection of information associated with, for example, the requirements of Rules 302, 303 and 304) as well as execute other platform capabilities and system operations. The estimated time burdens and costs for platform development discussed in this section include the estimated time

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(15,491 + 13,271+12,902+ 14,330+10,848) / 5 years). As of September 15, 2015, there were 4,213 broker-dealers registered with the Commission. Therefore, we estimate that there are approximately 3.17 amendments (13,368 amended Forms BD / 4,213 broker-dealers) per registered broker-dealer per year. We therefore estimate that the 10 broker-dealers who register under Regulation Crowdfunding will file, on aggregate, approximately 32 amendments per year.

1665 We have altered our cost estimates slightly from the Proposing Release (from $25,130 to $25,179) and note that the amended estimates are consistent with our recent estimates of what it would cost other types of nonresident entities to retain an agent for service of process and provide an opinion of counsel. *See* Registration Process for Security-Based Swap Dealers and Major Security-Based Swap Participants, Exchange Act Release No. 34-75611, 80 FR 48964, 48994 (Aug. 14, 2015). We inadvertently included the costs to non-resident funding portals of completing Schedule C in the Proposing Release. We anticipate, however, that nonresident funding portals will incur a time burden rather than a cost burden to complete Schedule C.

burdens and costs for the functionalities that will allow funding portals to comply with their disclosure, communication channel, and investor notification requirements.[1666]

Intermediaries that develop their platforms in-house will incur an initial time burden associated with setting up their systems. Based on our discussions with potential intermediaries prior to the publication of our proposed rules, we estimate that intermediaries creating the initial platform in-house will typically have a team of approximately four to six developers that will work on all aspects of platform development, including, but not limited to, front-end programming, data management, systems analysis, communication channels, document delivery, and Internet security.[1667] We estimate, based on our discussions with potential intermediaries prior to the publication of our proposed rules, that in developing a platform in-house, intermediaries will spend an average of 1,500 hours for planning, programming, and implementation.[1668]

It is difficult to estimate the number of intermediaries that will develop their initial platforms in-house, but assuming that half of the 110 newly-registered intermediaries[1669] do so, the total initial time burden on those intermediaries will be 82,500 hours (55 intermediaries x 1,500 hours = 82,500 hours).

We estimate that annually updating the features and functionality of an intermediary's platform will require approximately 20% of the hours required to initially develop the platform, for an average burden of 300 hours per year. If we assume that half of the 110 crowdfunding

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1666 *See* Sections IV.C.2.g. and IV.C.2.h.

1667 *See* Sections IV.C.2.g. and IV.C.2.h.

1668 This average takes into account intermediaries that will develop a brand new platform and those that will modify an existing platform to function in accordance with Regulation Crowdfunding.

1669 As discussed above, we anticipate that 10 intermediaries will newly register as brokers, 50 intermediaries will be brokers that are already registered, and 50 intermediaries will register as funding portals.

intermediaries update their systems accordingly each year, the total ongoing time burden will be 16,500 hours per year (55 intermediaries x 300 hours = 16,500 hours).

(2) Cost

There will be a cost associated with developing a platform for an intermediary that hires a third-party to develop its platform rather than developing it in-house. Based on our discussions with potential intermediaries prior to the publication of our proposed rules, we estimate that it will cost an intermediary approximately $250,000 to $600,000[1670] to build a new Internet-based crowdfunding portal and all of its basic functionality.[1671] Assuming that half of the 110 newly-registered intermediaries hire outside developers to build or to tailor their platforms, the total initial cost will range from $13,750,000 to $33,000,000 (55 intermediaries x $250,000 = $13,750,000; 55 intermediaries x $600,000 = $33,000,000). For purposes of this PRA analysis, we estimate the cost to be $23,375,000 (the average of $13,750,000 and $33,000,000).

We estimate that it will typically cost an intermediary approximately one-fifth of the initial development cost per year to use a third-party developer to provide annual maintenance on an Internet-based crowdfunding portal, including updating and basic functionality, or $85,000 per year on average.[1672] If we assume that half of the 110 crowdfunding intermediaries updated their

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1670 *See, e.g.*, ASSOB Letter (suggesting that the cost to establish a funding portal would run at least $480,000, which is within the range of our estimate).

1671 We anticipate that some percentage of intermediaries will already have in place platforms and related systems that will need to be tailored to comply with the requirements of Title III of the JOBS Act and Regulation Crowdfunding. We anticipate that these intermediaries will hire outside developers to tailor their platforms. We estimate an average cost of approximately $250,000 in the first year in order to tailor the current systems for an intermediary that already has in place a platform and related systems. Thus, this amount is already covered in our range of costs above -- $250,000 to $600,000.

1672 Our estimate of the average initial external cost per intermediary to develop a crowdfunding platform is the average of the cited range of $250,000 to $600,000, or $425,000 (($250,000 + $600,000)/ 2). One-fifth of the cost of $425,000 is $85,000.

systems accordingly, the total ongoing cost will be $4,675,000 per year (55 intermediaries x $85,000 = $4,675,000).

c. Measures to Reduce the Risk of Fraud

(1) Time Burden

The final rules will require intermediaries to have a reasonable basis for believing that an issuer seeking to offer and sell securities in reliance on Section 4(a)(6) through the intermediary's platform complies with the requirements in Section 4A(b) and the related requirements in Regulation Crowdfunding.[1673] The final rules will also require intermediaries to have a reasonable basis for believing that an issuer has established means to keep accurate records of the holders of the securities it will offer and sell through the intermediary's platform.[1674] For both requirements, an intermediary may reasonably rely on the representations of the issuer, unless the intermediary has reason to question the reliability of those representations. For the purposes of this PRA analysis, we expect that 100% of intermediaries will rely on the representations of issuers. Based on our industry knowledge and discussions with participants prior to the publication of our proposed rules, we calculate that this requirement will impose a time burden in the first year of five hours per intermediary to establish standard representations it will request from issuers, and six minutes per intermediary per issuer to obtain the issuer representation, which is consistent with estimates we have used for other regulated entities to obtain similar documentation, such as consents, from customers.

Based on our estimate that there will be approximately 1,900 offerings per year, that each issuer will conduct one offering per year, and that there will be 110 intermediaries, we estimate

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[1673] *See* Rule 301(a) of Regulation Crowdfunding.

[1674] *See* Rule 301(b) of Regulation Crowdfunding.

that each intermediary will facilitate an average of approximately 17 offerings per year (1,900 offerings/(10 newly registered broker-dealers + 50 previously registered broker-dealers + 50 funding portals)). Therefore, we estimate that the total initial burden hours will be approximately 740 hours ((5 hours/intermediary x (10 newly-registered broker-dealers + 50 previously-registered broker-dealers + 50 funding portals)) + (0.1 hours/issuer x 17 offerings x 110 intermediaries).

We believe that the ongoing time burdens for this requirement will be approximately one hour per intermediary per year to review and confirm that the standard representations it requests from issuers remain appropriate, and six minutes (0.1 hours) per intermediary per issuer to obtain an issuer's representation. Therefore, we estimate that the ongoing total burden hours necessary for intermediaries to rely on the representations of the issuers will be approximately 300 hours per year ((1 hour/intermediary x (10 newly-registered broker-dealers + 50 previously-registered broker-dealers + 50 funding portals)) + (0.1 hours/issuer x 17 offerings x 110 intermediaries).

(2) Cost

The final rules will require intermediaries to conduct a background and securities enforcement regulatory history check on each issuer and each officer, director or 20 Percent Beneficial Owner of an issuer to determine whether the issuer or such person is subject to a disqualification. We anticipate that most intermediaries will employ third parties to perform background and securities enforcement regulatory history checks in light of the costs of developing an in-house capability to conduct such checks. Therefore, for the purposes of this PRA analysis, we assume that 100% of intermediaries will use these third-party service providers.

The cost for a third party to perform a background check is estimated to be between $200 and $500, depending on the nature and extent of the information provided.[1675] We recognize that some issuers will require more than one background check (*e.g.*, for officers or directors of the issuer), and we estimate that intermediaries will perform four background checks per issuer, on average. We base this number on the assumption that most crowdfunding issuers will be startups and small businesses with small management teams and few owners. Assuming an average of approximately 1,900 offerings made in reliance on Section 4(a)(6) per year, the total estimated initial cost for all intermediaries to fulfill the required background and securities enforcement regulatory history checks will range from approximately $1,520,000 to $3,800,000 per year,[1676] or approximately $13,818 to $34,546 per intermediary per year.[1677] For purposes of this PRA analysis, we average this cost to $24,182 per intermediary per year.

One commenter noted, as a general matter, that the "costs incurred by the intermediary in dealing with an issuer, doing the required due diligence and background screening, establishing a web page describing the offering and so on do not vary linearly with the offering size. As a percentage of the offering amount, they will be disproportionately high for smaller offerings."[1678] This commenter did not, however, question our underlying assumptions or our estimates of these costs. For purposes of this PRA analysis and as discussed above, we believe that these cost

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1675 *See, e.g.*, A Matter of Fact, *Background Check FAQ: Frequently Asked Questions*, *available at* http://www.amof.info/faq.htm (Matter of Fact is a background check provider accredited by the National Association of Professional Background Screeners and the Background Screening Credentialing Council. This source states that the cost for a comprehensive background check is $200 to $500).

1676 1,900 securities-based offerings made in reliance on Section 4(a)(6) per year x ($200 to $500 per background and securities enforcement regulatory history check) x 4 checks per offering = $1,520,000 to $3,800,000 per year.

1677 $1,520,000/110 intermediaries = approximately $13,818 per intermediary; $3,800,000/110 intermediaries = approximately $34,546 per intermediary.

1678 Heritage Letter.

estimates are reasonable. We also believe that intermediaries are in a better position to make their own business decisions as to whether such costs would be disproportionately high for smaller offerings.[1679]

We believe that, on an ongoing basis, intermediaries will continue to use third-party services to conduct background and securities enforcement regulatory history checks. We also believe that the total estimated ongoing cost for all intermediaries to fulfill the required background and securities enforcement regulatory history checks will be the same as the estimated initial cost, or on average $24,182 per intermediary per year.

d. Account Opening: Accounts and Electronic Delivery

The final rules provide that no intermediary or associated person of an intermediary may accept an investment commitment in a transaction involving the offer or sale of securities made in reliance on Section 4(a)(6) until an investor has opened an account with the intermediary and consented to electronic delivery of materials.[1680] This requirement will impose certain information gathering and recordkeeping burdens on intermediaries. For the purposes of this PRA analysis, we expect that the functionality required to allow an investor to open an account with an intermediary and obtain consents will result in an initial time burden of approximately 10 hours per intermediary in the first year. Therefore, we estimate that the total initial burden hours resulting from this functionality will be approximately 1,100 hours (10 hours/intermediary x (10 newly-registered broker-dealers + 50 previously-registered broker-dealers + 50 funding portals)).

1679 As noted above, we agree with the commenter's suggestion that there is likely to be a fixed component to these costs that reflects a certain necessary level of due diligence and background screening, which will result in these costs, as a percentage of offering size, being higher for smaller offerings.

1680 *See* Rule 302(a) of Regulation Crowdfunding.

We believe that the ongoing time burdens for this requirement will be significantly less than the initial time burden, and thus we estimate approximately two hours per intermediary per year to review and assess the related processes. Therefore, we estimate that the ongoing total burden hours necessary for this functionality will be approximately 220 hours per year (2 hours/intermediary x (10 newly-registered broker-dealers + 50 previously-registered broker-dealers + 50 funding portals)).

e. Account Opening: Educational Materials

(1) Time Burden

The final rules require intermediaries to provide educational materials to investors,[1681] about the risks and costs of investing in securities offered and sold in reliance on Section 4(a)(6). Because the intermediary will determine what electronic format will prove most effective in communicating the requisite contents of the educational material, the expected costs for intermediaries to develop the educational material are expected to vary widely and are difficult to estimate. For the purposes of this PRA analysis, we assume that half of the intermediaries will develop their educational materials in-house, potentially including online presentations and written documents, and that the other half will employ third parties to produce educational materials, such as professional-quality online video presentations. We estimate that to develop their educational materials in-house, each intermediary will incur an initial time burden of approximately 20 hours. Therefore, the total initial burden will be approximately 1,100 hours (55 intermediaries x 20 hours/intermediary).[1682]

1681 *See* Rule 302(b) of Regulation Crowdfunding.

1682 In the Proposing Release we did not take into account in our estimated time burden and cost calculations our assumption that half of the intermediaries would develop educational materials in-house. Therefore, we have

Assuming that half of the intermediaries will develop their educational materials in-house, we also expect that these intermediaries will update their educational materials in-house, as needed. We estimate that to update their educational materials in-house, each intermediary will incur an ongoing time burden of approximately 10 hours per year. Therefore, the total ongoing burden will be approximately 550 hours per year (55 intermediaries x 10 hours/intermediary).

(2) Cost

As stated above, for the purposes of this PRA analysis, we assume that half of the intermediaries will employ third-party firms to produce educational materials, such as professional-quality online video presentations, instead of developing materials in-house. Public sources indicate that the typical cost to produce a professional corporate training video ranges from approximately $1,000 to $3,000 per production minute.[1683] Based on discussions with industry participants prior to the publication of our proposed rules, we assume that, on average, each intermediary will produce a series of short educational videos that will cover all of the requirements of the final rules and that the video material will be 10 minutes long in total. Based on this assumption, we estimate that the average initial cost for an intermediary to develop and produce educational materials will range from approximately $10,000 to $30,000. The total initial cost across all intermediaries estimated to employ a third party per year will be $550,000 to $1,650,000.[1684] For purposes of this PRA analysis, we average the cost to $20,000 per intermediary per year. We note that the estimated initial cost may be significantly lower, because

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re-calculated the estimated total initial and ongoing time burdens and costs for the development of in-house materials in this release based on 55 (rather than 110) intermediaries.

1683 *See, e.g.*, Lee W. Frederiksen, *What Is the Cost of Video Production for the Web?*, Hinge Marketing, *available at* http://www.hingemarketing.com/library/article/what-is-the-cost-of-video-production-for-the-web.

1684 55 intermediaries x $10,000 production cost = $550,000. 55 intermediaries x $30,000 production cost = $1,650,000.

not all intermediaries that outsource the development of educational materials may choose to produce professional-quality online video presentations; others may produce videos of shorter length or use other types of educational materials.

We estimate that, on an ongoing basis, when using a third-party company to update their video educational materials, each intermediary will spend approximately half of the initial average cost. We estimate, therefore, that the average ongoing annual cost for an intermediary to update its video educational materials will range from approximately $5,000 to $15,000 and that the total ongoing annual cost across all intermediaries will range from approximately $275,000 to $825,000 per year.[1685] For purposes of this PRA analysis, we average the cost to $10,000 per intermediary per year.

f. Account Opening: Promoters

The final rules require an intermediary, at the account opening stage, to disclose to users of its platform that any person who receives compensation to promote an issuer's offering, or who is a founder or employee of an issuer engaging in promotional activities on behalf of the issuer, must clearly disclose the receipt of compensation and his or her engagement in promotional activities on the platform.[1686] We expect that this requirement will result in an estimated time burden of five hours per intermediary in the first year, to prepare this particular disclosure and incorporate it into the account opening process. Therefore, we estimate that the total initial burden hours necessary for intermediaries to comply with this requirement will be approximately 550 hours (5 hours/intermediary x (10 newly-registered broker-dealers + 50 previously-registered broker-dealers + 50 funding portals)).

[1685] $550,000 total cost x 0.50 = $275,000. $1,650,000 total cost x 0.50 = $825,000.

[1686] *See* Rule 302(c) of Regulation Crowdfunding.

We believe that the ongoing time burdens for this requirement will be approximately one hour per intermediary per year to review and check that the disclosures remain appropriate. Therefore, we estimate that the ongoing total burden hours necessary for intermediaries to comply with this requirement will be approximately 110 hours per year (1 hour/intermediary x (10 newly-registered broker-dealers + 50 previously-registered broker-dealers + 50 funding portals)).

g. Issuer Disclosures to be Made Available

(1) Time Burden

The final rules require an intermediary to make publicly available on its platform the information that an issuer of crowdfunding securities is required to provide to investors, in a manner that reasonably permits a person accessing the platform to save, download or otherwise store the information, until the offer and sale of securities is completed or cancelled.[1687]

For purposes of the PRA, our estimate of the hourly burdens related to the public availability of the issuer information is included in our estimate of the hourly burdens associated with overall platform development, discussed above in Section IV.C.2.b. We note that the platform functionality will include not only the ability to display, upload and download issuer information as required under the final rules, but also the ability to provide users with required online disclosures

We recognize that, over time, intermediaries may need to update their systems that allow issuer information to be uploaded to their platforms. We do not expect a significant ongoing burden related to the requirement for providing issuer disclosures, primarily because the

[1687] *See* Rule 303(a) of Regulation Crowdfunding.

functionality required for required issuer disclosure information to be uploaded is a standard feature offered on many websites and will not require frequent or significant updates.

(2) Cost

We do not expect a significant ongoing cost for providing issuer disclosures, primarily because the functionality required to upload required issuer disclosure information is a standard feature offered on many websites and will not require frequent updates. To the extent an intermediary uses a third party to develop the functionality for this requirement, the initial costs relevant to this requirement will be incorporated into the cost of hiring a third party to develop the platform, discussed above in subsection IV.C.2.b.2.

h. Other Disclosures to Investors

(1) Time Burden

Intermediaries will be required to implement and maintain systems to comply with the information disclosure, communication channels, and investor notification requirements of Regulation Crowdfunding, including providing disclosure about compensation at account opening, obtaining investor acknowledgments to confirm investor qualifications and review of educational materials, providing investor questionnaires, maintaining communication channels with third parties and among investors, notifying investors of investment commitments, confirming completed transactions and confirming or reconfirming offering cancellations.

For purposes of the PRA analysis, our estimate of the hourly burdens related to these information disclosure, communication channel and investor notification requirements of Regulation Crowdfunding is included in our estimate of the hourly burdens associated with overall platform development, discussed above in Section IV.C.2.b. Based on our discussions with industry participants, we expect that these functionalities will generally be part of the overall

platform development process and costs. We discuss the burdens of platform development above, and note that these will include developing the functionality that will allow intermediaries to comply with disclosure and notification requirements.[1688]

We do not expect a significant ongoing burden for providing disclosures, as required by the final rules, because the functionality required to provide information and communication channels will likely not require frequent updates. We incorporate the total burden to update the required functionality for processing investor disclosures and investor acknowledgment information in the total burden estimates relating to platform development discussed above.[1689]

(2) Cost

We recognize that some intermediaries may implement the required functionality for processing investor disclosures and investor acknowledgments by using a third-party developer. The total cost for issuers to use third-party developers to add the required functionality for processing investor disclosures and investor acknowledgments, as well as to update the required functionality for processing investor disclosures and investor acknowledgments, is incorporated into our discussion of the total cost estimates relating to platform development in Section IV.C.2.b.

We also do not expect there to be a significant ongoing cost for developing the functionality to process these disclosures and acknowledgments, primarily because this functionality will likely not require frequent updates by third-party developers.

1688 *See* Section IV.C.2.b.1.

1689 *See* Section IV.C.2.b.1.

i. Maintenance and Transmission of Funds

The final rules contain requirements related to the maintenance and transmission of funds. A registered broker will be required to comply with the requirements of Rule 15c2-4 of the Exchange Act (Transmission or Maintenance of Payments Received in Connection with Underwritings).[1690] A registered funding portal will be required to enter into a written agreement with a qualified third party that has agreed in writing to hold the client funds.[1691] It also will be required to send directions to the qualified third party depending on whether an investing target is met or if an investment commitment or offering is cancelled. For purposes of the PRA, we are providing an estimate for the hour burden that a funding portal will incur to enter into a written agreement with the qualified third party on an initial basis, and to review and update that agreement on an ongoing basis.

Based on discussion with industry participants, we estimate that funding portals will incur an initial burden of approximately 20 hours each to comply with these requirements, for a total burden of 1,000 hours (20 hours per funding portal x 50 funding portals). We expect that the burden associated with the website functionality required to send directions to third parties will be included as part of the platform development discussed above.[1692]

We expect that, on an ongoing basis, a registered funding portal will have to periodically review and update its written agreement with the qualified third party to hold its client funds. A registered funding portal will also be required to send directions on an ongoing basis to a qualified

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1690 *See* Rule 303(e)(1) of Regulation Crowdfunding. *See also* 17 CFR 240.15c2-4. For purposes of this PRA discussion, any burdens associated with Rule 15c2-4, as well as for any other rule to which brokers are subject regardless of whether they engage in transactions pursuant to Section 4(a)(6), are not addressed here; rather, they are included in any OMB approvals for the relevant rules.

1691 *See* Rule 303(e)(2) of Regulation Crowdfunding.

1692 *See* Section IV.C.2.b.

third party depending on whether an investing target is met or an investment commitment or offering is cancelled. Based on discussion with industry participants, we estimate that funding portals will incur an ongoing annual burden of approximately 5 hours each to comply with these requirements, or 250 hours total (5 hours per funding portal x 50 funding portals).

j. Compliance: Policies and Procedures

The final rules require a funding portal to implement written policies and procedures reasonably designed to achieve compliance with the federal securities laws and the rules and regulations thereunder, relating to its business as a funding portal. We anticipate that funding portals will comply with this requirement by using internal personnel and internal information technology resources integrated into their platforms. Based on discussion with industry participants, we estimate that a funding portal will spend approximately 40 hours to establish written policies and procedures to achieve compliance with these requirements. This will result in a total aggregate initial recordkeeping burden of 2,000 hours (40 hours x 50 funding portals).

We estimate that, on an ongoing basis, funding portals will spend approximately 5 hours per year updating, as necessary, the policies and procedures required by the final rules. This will result in an aggregate ongoing recordkeeping burden of 250 hours (5 hours x 50 funding portals).

k. Compliance: Privacy

Funding portals will be required to comply with the Privacy Rules as they apply to broker-dealers, including Regulation S-P, S-AM and S-ID.[1693]

Under Rule 403(b), a funding portal will be required to comply with Regulation S-P, which will require the funding portal to provide notice to investors about its privacy policies and practices; describe the conditions under which a broker may disclose nonpublic personal

[1693] *See* Rule 403(b) of Regulation Crowdfunding.

information about investors to nonaffiliated third parties; and provide a method for investors to prevent a funding portal from disclosing that information to most nonaffiliated third parties by "opting out" of that disclosure, subject to certain exceptions. For funding portals, we expect that the privacy and opt-out notices will be delivered electronically, thereby reducing the delivery burden as compared to paper delivery.

We estimate that under the final rules all 50 funding portals will be subject to the requirements of Regulation S-P pursuant to Rule 403(b). In developing an estimate of the burden relating to the Regulation S-P requirements under Rule 403(b), we have considered: (1) the minimal recordkeeping burden imposed by Regulation S-P;[1694] (2) the summary fashion in which information must be provided to investors in the privacy and opt-out notices required by Regulation S-P;[1695] and (3) the availability of the model privacy form and online model privacy form builder. Given these considerations, we estimate that each funding portal will spend, on an ongoing basis, an average of approximately 12 hours per year complying with the information collection requirement of Regulation S-P, for a total of approximately 600 annual burden-hours (12 hours/respondent x 50 funding portals).

Funding portals will be required to comply with Regulation S-AM, which will require funding portals to provide notice to each affected individual informing the individual of his or her right to prohibit such marketing before a receiving affiliate may make marketing solicitations based on the communication of certain consumer financial information from the broker. Based on our discussions with industry participants, we estimate that approximately 20 funding portals will

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1694 Regulation S-P has no recordkeeping requirement, and records relating to customer communications already must be made and retained by broker-dealers pursuant to other Commission rules. The estimates of the burdens relating to recordkeeping requirements for funding portals are discussed below in Section IV.C.2.l.

1695 The model privacy form adopted by the Commission and the other agencies in 2009, designed to serve as both a privacy notice and an opt-out notice, is only two pages.

have affiliations that will subject them to the requirements of Regulation S-AM under the final rules, and that they will incur an average one-time burden of one hour to review affiliate marketing practices, for a total of 20 burden hours (1 hour/respondent x 20 funding portals).

We estimate that these 20 funding portals will be required to provide notice and opt-out opportunities to consumers pursuant to the requirements of Regulation S-AM, as imposed by Rule 403(b), and that they will incur an average initial burden of 18 hours to do so, for a total estimated initial burden of 360 hours (18 hours/respondent x 20 funding portals). We also estimate that funding portals will incur an ongoing burden related to Regulation S-AM's requirements for providing notice and opt-out opportunities of approximately four hours per respondent per year. This burden will cover the creation and delivery of notices to new investors and the recording of any opt-outs that are received on an ongoing basis, for a total of approximately 80 annual burden-hours (4 hours/respondent x 20 funding portals).

Funding portals will be required to comply with rule S-ID, which will require funding portals to develop and implement a written identity theft prevention program that is designed to detect, prevent and mitigate identity theft in connection with certain existing accounts or the opening of new accounts. We estimate that the initial burden for funding portals to comply with the applicable portions of Regulation S-ID, as imposed by Rule 403(b), will be (1) 25 hours to develop and obtain board approval of a program; (2) four hours to train staff; and (3) two hours to conduct an initial assessment of relevant accounts, for a total of 31 hours per funding portal. We estimate that all 50 funding portals will incur these initial burdens, resulting in an aggregate time burden of 1,550 hours ((25 + 4 + 2 hours / respondent) x 50 funding portals).

With respect to the requirements of Rule 403(b) relating to Regulation S-ID, we estimate that the ongoing burden per year will include: (1) two hours to periodically review and update the

program, review and preserve contracts with service providers and review and preserve any documentation received from service providers; (2) four hours to prepare and present an annual report to a compliance director; and (3) two hours to conduct periodic assessments to determine if the entity offers or maintains covered accounts, for a total of eight hours, of which we estimate 7 seven hours will be spent by internal counsel and 1 one hour will be spent by a compliance director. We estimate that all 50 funding portals will incur these ongoing burdens, for a total ongoing burden 400 hours (8 hours/respondent x 50 funding portals).

l. Records to be Made and Kept by Funding Portals

(1) Time Burden

All funding portals will be required to make and keep records related to their activities to facilitate transactions in reliance on Section 4(a)(6) and the related rules.[1696] These books and records requirements are based generally on Exchange Act Rules 17a-3 and 17a-4, which apply to broker-dealers. To estimate the initial burden for funding portals, we base our analysis upon the current annual burdens of Rules 17a-3 and 17a-4.

We currently estimate the annual recordkeeping burden for broker-dealer compliance with Rule 17a-3 to be 394.16 hours per respondent, and the most recently approved annual recordkeeping burden for broker-dealer compliance with Rule 17a-4 to be 249 hours per respondent.

Given the more limited scope of a funding portal's business as compared to that of a broker, the more targeted scope of the books and records rules, and the fact that funding portals will be required to make, deliver and store records electronically, we expect the burden of the final rules will likely be less than that of Rules 17a-3 and 17a-4. For the purposes of the PRA, we

[1696] *See* Rule 404 of Regulation Crowdfunding.

assume that the recordkeeping burden, on average, for a funding portal to comply with the final rules will be 50% of the burdens of a broker-dealer to comply with Rules 17a-3 and 17a-4. Therefore, we estimate the initial burden to be approximately 325 hours per respondent,[1697] or 16,250 hours total (325 hours/respondent x 50 respondents). We expect the ongoing recordkeeping burden for funding portals will be the same as the initial burden because the requirements regarding maintaining such records will be consistent each year.

(2) Cost

We currently estimate the annual recordkeeping cost for broker-dealer compliance with Rule 17a-3 to be $5,706.67 per respondent. These ongoing recordkeeping costs reflect the costs of systems and equipment development. We currently estimate the annual recordkeeping cost for broker-dealer compliance with Rule 17a-4 to be $5,000 per respondent.

Given the more limited scope of a funding portal's business as compared to that of a broker, the more targeted scope of the books and records rules, and the fact that funding portals will be required to make, deliver and store records electronically, we expect the annual recordkeeping cost of the final rule requirements will likely be less than that of Rules 17a-3 and 17a-4. For purposes of the PRA, we assume that the annual recordkeeping cost on average for a funding portal to comply with the requirements that records be made and kept will be about 50% less than burdens of a broker-dealer to comply with Rules 17a-3 and 17a-4. We expect the initial recordkeeping cost for funding portals, therefore, to be approximately $5,350 per respondent,[1698] or $267,500 total ($5,350 per respondent x 50 respondents). We expect the ongoing

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[1697] 394.16 hours (recordkeeping burden for Rule 17a-3) + 249 hours (recordkeeping burden for Rule 17a-4) = 643.16 hours. 638.16 hours/2 = 321.58 hours.

[1698] $5,706.67 (recordkeeping cost for Rule 17a-3) + $5,000 (recordkeeping cost for Rule 17a-4) = $10,706.67. $10,706.67 / 2 = $5,353.34.

recordkeeping cost burden for funding portals will be the same as the initial burden because the requirements regarding maintaining such records will be consistent each year.

One commenter stated that "[u]nder the expectation that crowdfunding portals will be online operations and will almost certainly retain records through digital methods, the burden of collection should be minimal."[1699] We agree that digital recordkeeping can help to minimize costs, and our estimates reflect this assessment.

D. Collections of Information are Mandatory

The collections of information required under Rules 201 through 203 will be mandatory for all issuers. The collections of information required under Rules 300 through 304 will be mandatory for all intermediaries. The collections of information required under Rules 400 through 404 will be mandatory for all funding portals.

E. Confidentiality

Responses on Form C, Form C-A, Form C-U, Form C-AR and Form C-TR will not be kept confidential. Responses on Form ID will be kept confidential by the Commission, subject to a request under the Freedom of Information Act.[1700] Responses on Forms BD and Forms Funding Portal will not be kept confidential.

F. Retention Period of Recordkeeping Requirements

Issuers are not subject to recordkeeping requirements under Regulation Crowdfunding. Intermediaries that are brokers will be required to retain records and information relating to Regulation Crowdfunding for the required retention periods specified in Exchange Act Rule 17a-

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1699 Joinvestor Letter.

1700 5 U.S.C. 552. The Commission's regulations that implement the Freedom of Information Act are at 17 CFR 200.80 *et seq*.

4. Intermediaries that are funding portals will be required to retain records and information under Regulation Crowdfunding for the required retention periods specified in Rule 404.[1701]

V. FINAL REGULATORY FLEXIBILITY ACT ANALYSIS

The Commission has prepared the following Final Regulatory Flexibility Analysis ("FRFA"), in accordance with the provisions of the Regulatory Flexibility Act,[1702] regarding Regulation Crowdfunding. It relates to the rules for securities-based crowdfunding being adopted today. An Initial Regulatory Flexibility Analysis ("IRFA") was prepared in accordance with the Regulatory Flexibility Act and included in the Proposing Release.

A. Need for the Rule

The regulation is designed to implement the requirements of Title III of the JOBS Act. Title III added Securities Act Section 4(a)(6), which provides a new exemption from the registration requirements of Securities Act Section 5 for securities-based crowdfunding transactions, provided the transactions are conducted in the manner set forth in new Securities Act Section 4A. Section 4A includes requirements for issuers that offer or sell securities in reliance on the crowdfunding exemption, as well as for persons acting as intermediaries in those transactions. The rules prescribe requirements governing the offer and sale of securities in reliance on Section 4(a)(6) and provide a framework for the regulation of registered funding portals and brokers that act as intermediaries in the offer and sale of securities in reliance on Section 4(a)(6).

As discussed above, the crowdfunding provisions of the JOBS Act, which we implement through this regulation, are intended to help alleviate the funding gap and accompanying

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1701 *See* Rule 404 of Regulation Crowdfunding.

1702 5 U.S.C. 603.

regulatory concerns faced by small businesses by making relatively low dollar offerings of securities less costly and by providing crowdfunding platforms a means by which to facilitate the offer and sale of securities without registering as brokers, with a framework for regulatory oversight to protect investors.

B. Significant Issues Raised by Public Comments

In the Proposing Release, we requested comment on every aspect of the IRFA, including the number of small entities that would be affected by the proposed amendments, the existence or nature of the potential impact of the proposals on small entities discussed in the analysis, and how to quantify the impact of the proposed rules.

Some commenters expressed concern that the IRFA did not comply with the Regulatory Flexibility Act because it did not, in their view, adequately describe the costs of the proposed rule on small entities, and did not set forth significant alternatives which accomplish the rule's objectives and which minimize the significant economic impact of the proposal on small entities.[1703] These commenters recommended that the Commission republish for public comment a supplemental IRFA to address these concerns. One commenter stated that the IRFA did not set forth significant alternatives which accomplish the Commission's stated objectives because the IRFA only considered alternatives related to exempting small business from the proposed rules.[1704] One commenter believed that the Commission should exercise its discretion and

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[1703] *See* SBA Office of Advocacy Letter; NAHB Letter; Graves Letter.

[1704] *See* SBA Office of Advocacy Letter.

eliminate the need for two years of audited financial statements,[1705] whereas another commenter viewed the audit requirement as a "heavy-handed" regulatory approach.[1706]

Commenters suggested several alternatives which in their view could reduce costs while accomplishing the rule's objectives.[1707] Commenters suggested that the Commission use its discretion to raise the threshold amount above which issuers would be required to provide audited financial statements,[1708] with one commenter specifically recommending a threshold of $900,000.[1709] One commenter also suggested that the Commission adopt a "question and answer" format for nonfinancial disclosures similar to the format used in Regulation A offerings.[1710] This same commenter also recommended that the Commission could develop "standard, boilerplate disclosures" for some of the "more complicated" nonfinancial disclosures such as risk factors. This commenter stated that the nonfinancial disclosures are not required under the JOBS Act and encouraged the Commission to develop alternatives that would be less burdensome for small issuers. One commenter recommended that the Commission revise the ongoing financial reporting requirements for small issuers to require the disclosure of reviewed rather than audited financial statements, even if such issuers were previously required to disclose audited financial statements pursuant to Section 4A(b)(1)(D).[1711] This commenter also supported a requirement that issuers submit annually an updated statement of financial condition, similar in nature to an abbreviated management's discussion and analysis of financial condition and results of

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1705 *See* Guzik Letter.

1706 *See* Rockethub Letter.

1707 *See* Graves Letter; SBA Office of Advocacy Letter.

1708 *Id*.

1709 *See* Graves Letter.

1710 *See* SBA Office of Advocacy Letter.

1711 *See* Graves Letter.

operations.[1712] This commenter also suggested that issuers with total revenue below $5 million should be permitted to use either cash-based or accrual-based methods of accounting, so that businesses using cash accounting will not be required to create two sets of accounting records in order to access crowdfunding.[1713]

One commenter suggested that smaller entities tend to be more volatile and more illiquid than larger entities.[1714] This commenter explained that this illiquidity needs to be considered when crafting regulations for small entity intermediaries and small entity issuers. This commenter also stated that, regardless of whether an intermediary has internal compliance personnel, or uses a third party, these compliance costs ultimately will have to be borne by the investors and issuers using the intermediary service. Another commenter expressed concern that the statutory liability standard of Section 4A(c) will be particularly burdensome for funding portals and noted that the IRFA does not account for the large expense statutory liability will impose on intermediaries.[1715] Similarly, one commenter thought it was appropriate to apply the same level of liability that is reserved for issuers to broker-dealers, but not funding portals.[1716] This commenter urged the Commission to either eliminate liability for funding portals, or create regulatory alternatives for funding portals such as allowing them to limit the offerings on their platforms.[1717] One

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1712 *See Id.*

1713 *See Id.*

1714 *See* RocketHub Letter.

1715 *See* SBA Office of Advocacy Letter (stating that the liability standard is especially burdensome for funding portals because broker-dealers already have procedures in place for conducting due diligence on issuers in order to meet FINRA requirements, and funding portals will have to establish these procedures anew).

1716 *See* Graves Letter (stating that the Commission should recognize the difference in the ability of funding portals and registered broker-dealers to use discretion in selecting or curating offerings, and apply liability to each as appropriate).

1717 *Id.* (suggesting that funding portals should be allowed the discretion to exclude offerings from their platforms if they deem them to be overly risky, or if they view the offerings as having shortcomings that could be detrimental to investors).

commenter stated that the IRFA did not account for the cost of prohibiting funding portals from limiting the offerings on their platforms on the basis of subjective factors and suggested that the Commission create a safe harbor for funding portals that allows them to limit such offerings.[1718]

C. Small Entities Subject to the Rules

For purposes of the Regulatory Flexibility Act, under our rules, an issuer (other than an investment company) is a "small business" or "small organization" if it has total assets of $5 million or less as of the end of its most recently completed fiscal year and is engaged or proposing to engage in an offering of securities which does not exceed $5 million.[1719] We believe that many issuers seeking to offer and sell securities in reliance on Section 4(a)(6) will be at a very early stage of their business development and will likely have total assets of $5 million or less. Also, to qualify for the exemption under Section 4(a)(6), the amount raised by an issuer must not exceed $1 million in a 12-month period. Therefore, we estimate that all issuers who offer or sell securities in reliance on the exemption will be classified as a "small business" or "small organization."

For purposes of the Regulatory Flexibility Act when used with reference to a broker or dealer, the Commission has defined the term "small entity" to mean a broker-dealer that: (1) had total capital (net worth plus subordinated liabilities) of less than $500,000 on the date in the prior fiscal year as of which its audited financial statements were prepared pursuant to Rule 17a-5(d) or, if not required to file such statements, a broker or dealer that had total capital (net worth plus subordinated debt) of less than $500,000 on the last business day of the preceding fiscal year (or in the time that it has been in business if shorter); and (2) is not affiliated with any person (other

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[1718] *See* SBA Office of Advocacy Letter.

[1719] 17 CFR 230.157.

than a natural person) that is not a small business or small organization as defined in this release."[1720] Currently, based on FOCUS Report[1721] data, there are 871 broker-dealers that are classified as "small" entities for purposes of the Regulatory Flexibility Act.[1722] Because of some overlap in permitted functions of funding portals and brokers, we look to the definition of a small broker-dealer to quantify the estimated numbers of small funding portals that will likely register under the new regulation. Based on discussions with industry participants prior to the publication of the proposed rules, we estimate that, of the anticipated 50 funding portals we expect to register under the new regulation, 30 will be classified as "small" entities for purposes of the Regulatory Flexibility Act.

D. Projected Reporting, Recordkeeping and other Compliance Requirements

As discussed above, the final rules include reporting, recordkeeping and other compliance requirements. In particular, the final rules impose certain disclosure requirements on issuers offering and selling securities in a transaction relying on the exemption provided by Section 4(a)(6). The final rules require that issuers relying on the exemption provided by Section 4(a)(6) file with the Commission certain specified information about the issuer and the offering, including information about the issuer's contact information; directors, officers and certain beneficial owners; business and business plan; current number of employees; financial condition; target offering amount and the deadline to reach the target offering amount; use of proceeds from the offering and price or method for calculating the price of the securities being offered; ownership

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1720 17 CFR 240.0-10(c).

1721 FOCUS Reports, or "Financial and Operational Combined Uniform Single" Reports, are monthly, quarterly, and annual reports that broker-dealers generally are required to file with the Commission and/or self-regulatory organizations pursuant to Exchange Act Rule 17a-5 (17 CFR 240.17a-5).

1722 *See* 17 CFR 240.0-10(a).

and capital structure; material factors that make an investment in the issuer speculative or risky; indebtedness; description of other offerings of securities; and transactions with related parties. Issuers also will be required to file updates with the Commission to describe the progress of the issuer in meeting the target offering amount, unless the issuer relies on the intermediary to include this information on its platform, and to disclose the total amount of securities sold in the offering. In addition, any issuer that sells securities in reliance on Section 4(a)(6) also will be required to file with the Commission an annual report to update the previously provided disclosure about the issuer's contact information; directors, officers and certain beneficial owners; business and business plan; current number of employees; financial condition; ownership and capital structure; material factors that make an investment in the issuer speculative or risky; indebtedness; description of other offerings of securities; and transactions with related parties.

Intermediaries will be required to register with the Commission as either brokers or as funding portals. Intermediaries also will be required to provide quarterly reports to the Commission. Funding portals will be required to make and keep certain records in accordance with the rules. Registered broker-dealers are already required to make and keep certain records in accordance with existing Exchange Act Rules 17a-3 and 17a-4. In addition, the final rules impose specific compliance requirements on intermediaries, such as the maintenance of written policies and procedures.

In adopting this regulation, we took into account that the regulation, as mandated by the JOBS Act, aimed to address difficulties encountered by small entities. Accordingly, we designed the final rules for intermediaries, to the extent possible in light of investor protection concerns, with the needs and constraints of small entities in mind, including small intermediaries. We believe that the reporting, recordkeeping and other compliance requirements of the final rules

applicable to intermediaries will impact, in particular, small entities that decide to register as funding portals. We believe that most of these requirements will be performed by internal compliance personnel of the broker or funding portal, but we expect that at least some funding portals may decide to hire outside counsel and third-party service providers to assist in meeting the compliance requirements. Given the statutory limitations on crowdfunding, we believe that the potential impact of the final rules on larger brokers and funding portals will be proportionally less than on small brokers and small intermediaries.

E. Agency Action to Minimize Effect on Small Entities

In response to comments, the final rules include a number of changes from the proposal, many of which were made to minimize the effect of the rules on small entities. These changes are outlined in detail above in the discussions of the rules adopted.

1. Issuers

To address commenters' concerns about the cost of the rules to small issuers, we have considered the alternatives suggested by commenters and are adopting final rules which implement certain alternatives we believe will minimize the cost of the final rules to small issuers while also preserving necessary investor protection measures.

First, the final rules include an accommodation for issuers conducting an offering for the first time in reliance on Regulation Crowdfunding. Under the final rules, issuers conducting an offering of more than $500,000 but not more than $1,000,000 that have not previously sold securities in reliance on Section 4(a)(6) will not be required to provide audited financial statements, unless audited financial statements are otherwise available. Instead, the final rules permit these issuers to provide reviewed financial statements. As discussed above, this is a change from the proposal that is responsive to concerns raised by many commenters about the

expense of obtaining audited financial statements, especially for start-up issuers without a track record of successfully raising capital.[1723] We believe that requiring reviewed financial statements for issuers using Regulation Crowdfunding for the first time to raise more than $500,000 but not more than $1 million, rather than audited financial statements, will minimize costs for issuers while providing sufficient investor protection by maintaining the benefit of an independent review.

As suggested by one commenter,[1724] and as discussed above, the final Form C includes an optional question-and-answer format that issuers may elect to use to provide the disclosures that are not required to be filed in XML format. Issuers opting to use this format would prepare their disclosures by answering the questions provided and filing that disclosure as an exhibit to the Form C. Given our expectation that issuers engaged in offerings in reliance on Section 4(a)(6) will encompass a wide variety of industries at different stages of business development, we do not believe it would be practical or useful to develop standard, predetermined disclosure, as suggested by one commenter, for such a variety of issuers. Also, as discussed above, we do not believe that financial statements prepared in accordance with other comprehensive bases of accounting, such as cash or accrual-based accounting, as suggested by one commenter, provide investors with a fair representation of a company's financial position and results of operations, and it may be difficult for investors to determine whether the issuer complied with such basis. Although we acknowledge, as some commenters observed, that other bases of accounting may be less expensive than U.S. GAAP, we believe the benefit of a single standard that will facilitate comparison among securities-based crowdfunding issuers justifies any incremental expenses

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1723 *See, e.g.*, SBA Office of Advocacy Letter.

1724 *Id*.

associated with U.S. GAAP. We also note that financial statements prepared in accordance with U.S. GAAP are generally self-scaling to the size and complexity of the issuer, which we expect to reduce the burden of preparing financial statements for many early stage issuers, including small issuers.

The final rules also maintain the progress update requirement, but with a significant modification from the proposed rule which is intended to reduce duplicative disclosure and minimize the burden on small issuers. The final rules will require an issuer to file a Form C-U at the end of the offering to disclosure the total amount of securities sold in the offering, but the rules permit issuers to satisfy the 50% and 100% progress update requirements by relying on the relevant intermediary to make publicly available on the intermediary's platform frequent updates about the issuer's progress toward meeting the target offering amount.

With respect to ongoing reporting requirements, rather than requiring an issuer to provide financial statements in the annual report that meet the highest standard previously provided, as proposed, the final rules require financial statements of the issuer certified by the principal executive officer of the issuer to be true and complete in all material respects. We expect that reducing the required level of public accountant involvement will minimize the costs and burdens for all issuers, including small issuers, associated with preparing reviewed and audited financial statements on an ongoing basis.

In addition, the final rules provide for termination of the ongoing reporting obligation in two additional circumstances: (1) the issuer has filed at least one annual report and has fewer than 300 holders of record, or (2) the issuer has filed the annual reports for at least the three most recent years and has total assets not exceeding $10,000,000. We believe the addition of these

termination events should help reduce related costs for issuers that may not have achieved a level of financial success that would sustain an ongoing reporting obligation.

Overall, we considered whether to establish different compliance or reporting requirements or timetables or to clarify, consolidate or simplify compliance and reporting requirements for small issuers. As noted above, we have made significant revisions to the final rules to address commenters' concerns about compliance and reporting burdens faced by issuers, especially small issuers. With respect to using performance rather than design standards, we used performance standards to the extent appropriate under the statute. For example, issuers have the flexibility to customize the presentation of certain disclosures in their offering statements.[1725] We also considered whether there should be an exemption from coverage of the rule, or any part of the rule, for small issuers. However, because the rules have been designed to implement crowdfunding, which focuses on capital formation by issuers that are small entities, while at the same time provide appropriate investor protections, we do not believe that small issuers should be exempt, in whole or in part, from the proposed rules.

2. Intermediaries

In response to comments, we have made a number of changes from the proposal with respect to intermediaries that will help to alleviate the compliance burdens faced by small entities. Most significantly, and in response to commenters' concerns about the application of Section 4A(c) liability,[1726] as discussed above, Rule 402(b)(1) has been modified from the proposal to include a safe harbor that provides a funding portal the ability to determine whether and under what terms to allow an issuer to offer and sell securities in reliance on Section 4(a)(6) of the

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[1725] *See* Section II.B.3.

[1726] *See, e.g.*, SBA Office of Advocacy Letter.

Securities Act through its platform; provided that a funding portal otherwise complies with Regulation Crowdfunding. This change is expected to allow intermediaries, including small entities, to reduce their exposure to such liability by denying access to issuers that present risk of fraud or other investor protection concerns. In addition, in a change from the proposed rules, we are not requiring a fidelity bond for intermediaries and also are expanding the definition of qualified third party. These changes should reduce costs for all intermediaries, including small entities.

The final rules have been tailored to the more limited role intermediaries will play in offerings made pursuant to Securities Act Section 4(a)(6) (as compared to the wide range of services that a traditional broker-dealer may provide). Registered brokers and funding portals will engage in similar activities related to crowdfunding and must comply with the adopted rules. The effective date for the registration provisions for funding portals will allow funding portals to be in a position to engage in crowdfunding at the same time as registered brokers once the rest of the rules become effective. These effective dates are designed to accommodate competitiveness concerns related to funding portals' and registered broker dealers' abilities to begin crowdfunding concurrently. While registered broker-dealers may perform services that a funding portal is prohibited from performing, the Exchange Act and rules thereunder, as well as SRO rules, already govern those activities. Therefore, we believe that the adopted rules are appropriate and properly tailored for the permissible activities of all brokers and funding portals.

We also considered whether, for small brokers or small funding portals, to establish different compliance, reporting or timing requirements, or whether to clarify, consolidate or simplify those requirements in our rules. While the final rules are based in large part on existing compliance requirements applicable to registered brokers to the extent they are applicable to

activities permitted for funding portals, we do not believe we should establish different requirements for small entities (whether registered brokers or funding portals) that engage in crowdfunding because such activities are limited in scope and, as such, the adopted rules are tailored to that more limited activity.

VI. STATUTORY AUTHORITY AND TEXT OF PROPOSED REGULATION

We are adopting the rules and forms contained in this document under the authority set forth in the Securities Act (15 U.S.C. 77a *et seq.*), particularly, Sections 4(a)(6), 4A, 19 and 28 thereof; the Exchange Act (15 U.S.C. 78a *et seq.*), particularly, Sections 3(b), 3(h), 10(b), 15, 17, 23(a) and 36 thereof; and Pub. L. No. 112-106, §301-305, 126 Stat. 306 (2012).

List of Subjects

17 CFR Part 200

Administrative practice and procedure, Authority delegations (Government agencies), Organization and functions (Government agencies).

Reporting and recordkeeping requirements.

17 CFR Part 227

Crowdfunding, Funding Portals, Intermediaries, Reporting and recordkeeping requirements, Securities.

17 CFR Parts 232 and 239

Reporting and recordkeeping requirements, Securities.

17 CFR Part 240

Brokers, Confidential business information, Fraud, Reporting and recordkeeping requirements, Securities.

17 CFR Part 249

Brokers, Reporting and recordkeeping requirements, Securities.

In accordance with the foregoing, title 17, chapter II of the Code of Federal Regulations is amended as follows:

PART 200 – ORGANIZATION; CONDUCT AND ETHICS; AND INFORMATION AND REQUESTS

SUBPART A – Organization and Program Management

1. The authority citation for Part 200, Subpart A, continues to read, in part as follows:

Authority: 15 U.S.C. 77c, 77o, 77s, 77z-3, 77sss, 78d, 78d-1, 78d-2, 78o-4, 78w, 78ll(d), 78mm, 80a-37, 80b-11, 7202, and 7211 et seq., unless otherwise noted.

* * * * *

2. Amend § 200.30-1 by:

a. Redesignating paragraphs (d), (e), (f), (g), (h), (i), (j) and (k) as paragraphs (e), (f), (g), (h), (i), (j), (k) and (*l*), respectively; and

b. Adding new paragraph (d).

The addition reads as follows:

§ 200.30-1 Delegation of authority to Director of Division of Corporation Finance.

* * * * *

(d) With respect to the Securities Act of 1933 (15 U.S.C. 77a *et seq*.) and §§ 227.100 through 227.503 of this chapter, to authorize the granting of applications under § 227.503(b)(2) of this chapter upon the showing of good cause that it is not necessary under the circumstances that the exemption under Regulation Crowdfunding be denied.

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PART 227—REGULATION CROWDFUNDING, GENERAL RULES AND REGULATIONS

3. The authority citation for Part 227 reads as follows:

Authority: 15 U.S.C. 77d, 77d-1, 77s, 78c, 78o, 78q, 78w, 78mm, and Pub. L. No. 112-106, §301-305, 126 Stat. 306 (2012).

4. Part 227 is added to read as follows:

Sec.

REGULATION CROWDFUNDING

Subpart A General

227.100 Crowdfunding exemption and requirements.

Subpart B Requirements for Issuers

227.201 Disclosure requirements.

227.202 Ongoing reporting requirements.

227.203 Filing requirements and form.

227.204 Advertising.

227.205 Promoter compensation.

Subpart C Requirements for Intermediaries

227.300 Intermediaries.

227.301 Measures to reduce risk of fraud.

227.302 Account opening.

227.303 Requirements with respect to transactions.

227.304 Completion of offerings, cancellations and reconfirmations.

227.305 Payments to third parties.

Subpart D Funding Portal Regulation

227.400 Registration of funding portals.

227.401 Exemption.

227.402 Conditional safe harbor.

227.403 Compliance.

227.404 Records to be made and kept by funding portals.

Subpart E Miscellaneous Provisions

227.501 Restrictions on resales.

227.502 Insignificant deviations from a term, condition or requirement of Regulation Crowdfunding.

227.503 Disqualification provisions.

SUBPART A – General

§ 227.100 Crowdfunding exemption and requirements.

(a) *Exemption*. An issuer may offer or sell securities in reliance on Section 4(a)(6) of the Securities Act of 1933 (the "Securities Act") (15 U.S.C. 77d(a)(6)), provided that:

(1) The aggregate amount of securities sold to all investors by the issuer in reliance on Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)) during the 12-month period preceding the date of such offer or sale, including the securities offered in such transaction, shall not exceed $1,000,000;

(2) The aggregate amount of securities sold to any investor across all issuers in reliance on Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)) during the 12-month period preceding the date of such transaction, including the securities sold to such investor in such transaction, shall not exceed:

(i) The greater of $2,000 or 5 percent of the lesser of the investor's annual income or net

worth if either the investor's annual income or net worth is less than $100,000; or

(ii) 10 percent of the lesser of the investor's annual income or net worth, not to exceed an amount sold of $100,000, if both the investor's annual income and net worth are equal to or more than $100,000;

Instruction 1 to paragraph (a)(2). To determine the investment limit for a natural person, the person's annual income and net worth shall be calculated as those values are calculated for purposes of determining accredited investor status in accordance with § 230.501 of this chapter.

Instruction 2 to paragraph (a)(2). A person's annual income and net worth may be calculated jointly with that person's spouse; however, when such a joint calculation is used, the aggregate investment of the investor spouses may not exceed the limit that would apply to an individual investor at that income or net worth level.

Instruction 3 to paragraph (a)(2). An issuer offering and selling securities in reliance on Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)) may rely on the efforts of an intermediary required by § 227.303(b) to ensure that the aggregate amount of securities purchased by an investor in offerings pursuant to Section 4(a)(6) of the Securities Act will not cause the investor to exceed the limit set forth in Section 4(a)(6) of the Securities Act and § 227.100(a)(2), *provided that* the issuer does not know that the investor has exceeded the investor limits or would exceed the investor limits as a result of purchasing securities in the issuer's offering.

(3) The transaction is conducted through an intermediary that complies with the requirements in Section 4A(a) of the Securities Act (15 U.S.C. 77d-1(a)) and the related requirements in this part, and the transaction is conducted exclusively through the intermediary's platform; and

Instruction to paragraph (a)(3). An issuer shall not conduct an offering or concurrent

offerings in reliance on Section 4(a)(6) of the Securities Act of 1933 (15 U.S.C. 77d(a)(6)) using more than one intermediary.

(4) The issuer complies with the requirements in Section 4A(b) of the Securities Act (15 U.S.C. 77d-1(b)) and the related requirements in this part; *provided, however,* that the failure to comply with §§ 227.202, 227.203(a)(3) and 227.203(b) shall not prevent an issuer from relying on the exemption provided by Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)).

(b) *Applicability*. The crowdfunding exemption shall not apply to transactions involving the offer or sale of securities by any issuer that:

(1) Is not organized under, and subject to, the laws of a State or territory of the United States or the District of Columbia;

(2) Is subject to the requirement to file reports pursuant to Section 13 or Section 15(d) of the Securities Exchange Act of 1934 (the "Exchange Act") (15 U.S.C. 78m or 78o(d));

(3) Is an investment company, as defined in Section 3 of the Investment Company Act of 1940 (15 U.S.C. 80a-3), or is excluded from the definition of investment company by Section 3(b) or Section 3(c) of that Act (15 U.S.C. 80a-3(b) or 80a-3(c));

(4) Is not eligible to offer or sell securities in reliance on Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)) as a result of a disqualification as specified in § 227.503(a);

(5) Has sold securities in reliance on Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)) and has not filed with the Commission and provided to investors, to the extent required, the ongoing annual reports required by this part during the two years immediately preceding the filing of the required offering statement; or

Instruction to paragraph (b)(5). An issuer delinquent in its ongoing reports can again rely on Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)) once it has filed with the

Commission and provided to investors both of the annual reports required during the two years immediately preceding the filing of the required offering statement.

(6) Has no specific business plan or has indicated that its business plan is to engage in a merger or acquisition with an unidentified company or companies.

(c) *Issuer*. For purposes of §227.201(r), calculating aggregate amounts offered and sold in §227.100(a) and §227.201(t), and determining whether an issuer has previously sold securities in §227.201(t)(3), *issuer* includes all entities controlled by or under common control with the issuer and any predecessors of the issuer.

Instruction to paragraph (c). The term *control* means the possession, direct or indirect, of the power to direct or cause the direction of the management and policies of the entity, whether through the ownership of voting securities, by contract or otherwise.

(d) *Investor*. For purposes of this part, *investor* means any investor or any potential investor, as the context requires.

SUBPART B – Requirements for Issuers

§ 227.201 Disclosure requirements.

An issuer offering or selling securities in reliance on Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)) and in accordance with Section 4A of the Securities Act (15 U.S.C. 77d-1) and this part must file with the Commission and provide to investors and the relevant intermediary the following information:

(a) The name, legal status (including its form of organization, jurisdiction in which it is organized and date of organization), physical address and website of the issuer;

(b) The names of the directors and officers (and any persons occupying a similar status or performing a similar function) of the issuer, all positions and offices with the issuer held by such

persons, the period of time in which such persons served in the position or office and their business experience during the past three years, including:

(1) Each person's principal occupation and employment, including whether any officer is employed by another employer; and

(2) The name and principal business of any corporation or other organization in which such occupation and employment took place.

Instruction to paragraph (b). For purposes of this paragraph (b), the term *officer* means a president, vice president, secretary, treasurer or principal financial officer, comptroller or principal accounting officer, and any person routinely performing similar functions.

(c) The name of each person, as of the most recent practicable date but no earlier than 120 days prior to the date the offering statement or report is filed, who is a beneficial owner of 20 percent or more of the issuer's outstanding voting equity securities, calculated on the basis of voting power;

(d) A description of the business of the issuer and the anticipated business plan of the issuer;

(e) The current number of employees of the issuer;

(f) A discussion of the material factors that make an investment in the issuer speculative or risky;

(g) The target offering amount and the deadline to reach the target offering amount, including a statement that if the sum of the investment commitments does not equal or exceed the target offering amount at the offering deadline, no securities will be sold in the offering, investment commitments will be cancelled and committed funds will be returned;

(h) Whether the issuer will accept investments in excess of the target offering amount and, if so, the maximum amount that the issuer will accept and how oversubscriptions will be allocated, such as on a pro-rata, first come-first served, or other basis;

(i) A description of the purpose and intended use of the offering proceeds;

Instruction to paragraph (i). An issuer must provide a reasonably detailed description of any intended use of proceeds, such that investors are provided with enough information to understand how the offering proceeds will be used. If an issuer has identified a range of possible uses, the issuer should identify and describe each probable use and the factors the issuer may consider in allocating proceeds among the potential uses. If the issuer will accept proceeds in excess of the target offering amount, the issuer must describe the purpose, method for allocating oversubscriptions, and intended use of the excess proceeds with similar specificity.

(j) A description of the process to complete the transaction or cancel an investment commitment, including a statement that:

(1) Investors may cancel an investment commitment until 48 hours prior to the deadline identified in the issuer's offering materials;

(2) The intermediary will notify investors when the target offering amount has been met;

(3) If an issuer reaches the target offering amount prior to the deadline identified in its offering materials, it may close the offering early if it provides notice about the new offering deadline at least five business days prior to such new offering deadline (absent a material change that would require an extension of the offering and reconfirmation of the investment commitment); and

(4) If an investor does not cancel an investment commitment before the 48-hour period prior to the offering deadline, the funds will be released to the issuer upon closing of the offering and the investor will receive securities in exchange for his or her investment;

(k) A statement that if an investor does not reconfirm his or her investment commitment after a material change is made to the offering, the investor's investment commitment will be cancelled and the committed funds will be returned;

(l) The price to the public of the securities or the method for determining the price, provided that, prior to any sale of securities, each investor shall be provided in writing the final price and all required disclosures;

(m) A description of the ownership and capital structure of the issuer, including:

(1) The terms of the securities being offered and each other class of security of the issuer, including the number of securities being offered and/or outstanding, whether or not such securities have voting rights, any limitations on such voting rights, how the terms of the securities being offered may be modified and a summary of the differences between such securities and each other class of security of the issuer, and how the rights of the securities being offered may be materially limited, diluted or qualified by the rights of any other class of security of the issuer;

(2) A description of how the exercise of rights held by the principal shareholders of the issuer could affect the purchasers of the securities being offered;

(3) The name and ownership level of each person, as of the most recent practicable date but no earlier than 120 days prior to the date the offering statement or report is filed, who is the beneficial owner of 20 percent or more of the issuer's outstanding voting equity securities, calculated on the basis of voting power;

(4) How the securities being offered are being valued, and examples of methods for how such securities may be valued by the issuer in the future, including during subsequent corporate actions;

(5) The risks to purchasers of the securities relating to minority ownership in the issuer and the risks associated with corporate actions including additional issuances of securities, issuer repurchases of securities, a sale of the issuer or of assets of the issuer or transactions with related parties; and

(6) A description of the restrictions on transfer of the securities, as set forth in § 227.501;

(n) The name, SEC file number and Central Registration Depository (CRD) number (as applicable) of the intermediary through which the offering is being conducted;

(o) A description of the intermediary's financial interests in the issuer's transaction and in the issuer, including:

(1) The amount of compensation to be paid to the intermediary, whether as a dollar amount or a percentage of the offering amount, or a good faith estimate if the exact amount is not available at the time of the filing, for conducting the offering, including the amount of referral and any other fees associated with the offering, and

(2) Any other direct or indirect interest in the issuer held by the intermediary, or any arrangement for the intermediary to acquire such an interest;

(p) A description of the material terms of any indebtedness of the issuer, including the amount, interest rate, maturity date and any other material terms;

(q) A description of exempt offerings conducted within the past three years;

Instruction to paragraph (q). In providing a description of any prior exempt offerings, disclose:

(1) The date of the offering;

(2) The offering exemption relied upon;

(3) The type of securities offered; and

(4) The amount of securities sold and the use of proceeds;

(r) A description of any transaction since the beginning of the issuer's last fiscal year, or any currently proposed transaction, to which the issuer was or is to be a party and the amount involved exceeds five percent of the aggregate amount of capital raised by the issuer in reliance on Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)) during the preceding 12-month period, inclusive of the amount the issuer seeks to raise in the current offering under Section 4(a)(6) of the Securities Act, in which any of the following persons had or is to have a direct or indirect material interest:

(1) Any director or officer of the issuer;

(2) Any person who is, as of the most recent practicable date but no earlier than 120 days prior to the date the offering statement or report is filed, the beneficial owner of 20 percent or more of the issuer's outstanding voting equity securities, calculated on the basis of voting power;

(3) If the issuer was incorporated or organized within the past three years, any promoter of the issuer; or

(4) Any member of the family of any of the foregoing persons, which includes a child, stepchild, grandchild, parent, stepparent, grandparent, spouse or spousal equivalent, sibling, mother-in-law, father-in-law, son-in-law, daughter-in-law, brother-in-law, or sister-in-law, and shall include adoptive relationships. The term *spousal equivalent* means a cohabitant occupying a relationship generally equivalent to that of a spouse.

Instruction 1 to paragraph (r). For each transaction identified, disclose the name of the specified person and state his or her relationship to the issuer, and the nature and, where practicable, the approximate amount of his or her interest in the transaction. The amount of such interest shall be computed without regard to the amount of the profit or loss involved in the transaction. Where it is not practicable to state the approximate amount of the interest, the approximate amount involved in the transaction shall be disclosed.

Instruction 2 to paragraph (r). For purposes of paragraph (r), a transaction includes, but is not limited to, any financial transaction, arrangement or relationship (including any indebtedness or guarantee of indebtedness) or any series of similar transactions, arrangements or relationships.

(s) A discussion of the issuer's financial condition, including, to the extent material, liquidity, capital resources and historical results of operations;

Instruction 1 to paragraph (s).

The discussion must cover each period for which financial statements of the issuer are provided. An issuer also must include a discussion of any material changes or trends known to management in the financial condition and results of operations of the issuer subsequent to the period for which financial statements are provided.

Instruction 2 to paragraph (s). For issuers with no prior operating history, the discussion should focus on financial milestones and operational, liquidity and other challenges. For issuers with an operating history, the discussion should focus on whether historical results and cash flows are representative of what investors should expect in the future. Issuers should take into account the proceeds of the offering and any other known or pending sources of capital. Issuers also should discuss how the proceeds from the offering will affect the issuer's liquidity, whether receiving these funds and any other additional funds is necessary to the viability of the business,

and how quickly the issuer anticipates using its available cash. In addition, issuers should describe the other available sources of capital to the business, such as lines of credit or required contributions by shareholders.

Instruction 3 to paragraph (s). References to the issuer in this paragraph and its instructions refer to the issuer and its predecessors, if any.

(t) For offerings that, together with all other amounts sold under Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)) within the preceding 12-month period, have, in the aggregate, the following target offering amounts:

(1) $100,000 or less, the amount of total income, taxable income and total tax, or the equivalent line items, as reported on the federal income tax returns filed by the issuer for the most recently completed year (if any), which shall be certified by the principal executive officer of the issuer to reflect accurately the information reported on the issuer's federal income tax returns, and financial statements of the issuer, which shall be certified by the principal executive officer of the issuer to be true and complete in all material respects. If financial statements of the issuer are available that have either been reviewed or audited by a public accountant that is independent of the issuer, the issuer must provide those financial statements instead and need not include the information reported on the federal income tax returns or the certifications of the principal executive officer;

(2) More than $100,000, but not more than $500,000, financial statements of the issuer reviewed by a public accountant that is independent of the issuer. If financial statements of the issuer are available that have been audited by a public accountant that is independent of the issuer, the issuer must provide those financial statements instead and need not include the reviewed financial statements; and

(3) More than $500,000, financial statements of the issuer audited by a public accountant that is independent of the issuer; *provided, however*, that for issuers that have not previously sold securities in reliance on Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)), offerings that have a target offering amount of more than $500,000, but not more than $1,000,000, financial statements of the issuer reviewed by a public accountant that is independent of the issuer. If financial statements of the issuer are available that have been audited by a public accountant that is independent of the issuer, the issuer must provide those financial statements instead and need not include the reviewed financial statements.

Instruction 1 to paragraph (t).

To determine the financial statements required under this paragraph (t), an issuer must aggregate amounts sold in reliance on Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)) within the preceding 12-month period and the offering amount in the offering for which disclosure is being provided. If the issuer will accept proceeds in excess of the target offering amount, the issuer must include the maximum offering amount that the issuer will accept in the calculation to determine the financial statements required under this paragraph (t).

Instruction 2 to paragraph (t). An issuer may voluntarily meet the requirements of this paragraph (t) for a higher aggregate target offering amount.

Instruction 3 to paragraph (t). The financial statements must be prepared in accordance with U.S. generally accepted accounting principles and include balance sheets, statements of comprehensive income, statements of cash flows, statements of changes in stockholders' equity and notes to the financial statements. If the financial statements are not audited, they must be labeled as "unaudited." The financial statements must cover the two most recently completed fiscal years or the period(s) since inception, if shorter.

Instruction 4 to paragraph (t). For an offering conducted in the first 120 days of a fiscal year, the financial statements provided may be for the two fiscal years prior to the issuer's most recently completed fiscal year; however, financial statements for the two most recently completed fiscal years must be provided if they are otherwise available. If more than 120 days have passed since the end of the issuer's most recently completed fiscal year, the financial statements provided must be for the issuer's two most recently completed fiscal years. If the 120th day falls on a Saturday, Sunday, or holiday, the next business day shall be considered the 120th day for purposes of determining the age of the financial statements.

Instruction 5 to paragraph (t). An issuer may elect to delay complying with any new or revised financial accounting standard that applies to companies that are not issuers (as defined under section 2(a) of the Sarbanes-Oxley Act of 2002 (15 U.S.C. 7201(a)) until the date that such companies are required to comply with such new or revised accounting standard. Issuers electing this accommodation must disclose it at the time the issuer files its offering statement and apply the election to all standards. Issuers electing not to use this accommodation must forgo this accommodation for all financial accounting standards and may not elect to rely on this accommodation in any future filings.

Instruction 6 to paragraph (t). An issuer required to provide information from a tax return under paragraph (t)(1) of this section before filing a tax return with the U.S. Internal Revenue Service for the most recently completed fiscal year may provide information from its tax return for the prior year (if any), provided that the issuer provides information from the tax return for the most recently completed fiscal year when it is filed with the U.S. Internal Revenue Service (if the tax return is filed during the offering period). An issuer that requested an extension from the U.S. Internal Revenue Service would not be required to provide information from the tax return until

the date the return is filed, if filed during the offering period. If an issuer has not yet filed a tax return and is not required to file a tax return before the end of the offering period, then the tax return information does not need to be provided.

Instruction 7 to paragraph (t). An issuer providing financial statements that are not audited or reviewed and tax information as specified under paragraph (t)(1) of this section must have its principal executive officer provide the following certification:

I, [identify the certifying individual], certify that:

(1) the financial statements of [identify the issuer] included in this Form are true and complete in all material respects; and

(2) the tax return information of [identify the issuer] included in this Form reflects accurately the information reported on the tax return for [identify the issuer] filed for the fiscal year ended [date of most recent tax return].

[Signature and title].

Instruction 8 to paragraph (t). Financial statement reviews shall be conducted in accordance with the Statements on Standards for Accounting and Review Services issued by the Accounting and Review Services Committee of the American Institute of Certified Public Accountants. A signed review report must accompany the reviewed financial statements, and an issuer must notify the public accountant of the issuer's intended use of the review report in the offering. An issuer will not be in compliance with the requirement to provide reviewed financial statements if the review report includes modifications.

Instruction 9 to paragraph (t). Financial statement audits shall be conducted in accordance with either auditing standards issued by the American Institute of Certified Public Accountants (referred to as U.S. Generally Accepted Auditing Standards) or the standards of the

Public Company Accounting Oversight Board. A signed audit report must accompany audited financial statements, and an issuer must notify the public accountant of the issuer's intended use of the audit report in the offering. An issuer will not be in compliance with the requirement to provide audited financial statements if the audit report includes a qualified opinion, an adverse opinion, or a disclaimer of opinion.

Instruction 10 to paragraph (t). To qualify as a public accountant that is independent of the issuer for purposes of this part, the accountant must satisfy the independence standards of either:

(i) 17 CFR 210.2-01 of this chapter, or

(ii) The American Institute of Certified Public Accountants. The public accountant that audits or reviews the financial statements provided by an issuer must be:

(a) Duly registered and in good standing as a certified public accountant under the laws of the place of his or her residence or principal office; or

(b) In good standing and entitled to practice as a public accountant under the laws of his or her place of residence or principal office.

Instruction 11 to paragraph (t). Except as set forth in § 227.100(c), references to the issuer in this paragraph (t) and its instructions (2) through (10) refer to the issuer and its predecessors, if any.

(u) Any matters that would have triggered disqualification under § 227.503(a) but occurred before [INSERT DATE 180 DAYS AFTER PUBLICATION IN THE FEDERAL REGISTER]. The failure to provide such disclosure shall not prevent an issuer from continuing to rely on the exemption provided by Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)) if the issuer

establishes that it did not know and, in the exercise of reasonable care, could not have known of the existence of the undisclosed matter or matters;

Instruction to paragraph (u). An issuer will not be able to establish that it could not have known of a disqualification unless it has made factual inquiry into whether any disqualifications exist. The nature and scope of the factual inquiry will vary based on the facts and circumstances concerning, among other things, the issuer and the other offering participants.

(v) Updates regarding the progress of the issuer in meeting the target offering amount, to be provided in accordance with § 227.203;

(w) Where on the issuer's website investors will be able to find the issuer's annual report, and the date by which such report will be available on the issuer's website;

(x) Whether the issuer or any of its predecessors previously failed to comply with the ongoing reporting requirements of § 227.202; and

(y) Any material information necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading.

Instruction to §227.201. If disclosure provided pursuant to any paragraph of this section also satisfies the requirements of one or more other paragraphs of this section, it is not necessary to repeat the disclosure. Instead of repeating information, an issuer may include a cross-reference to disclosure contained elsewhere in the offering statement or report, including to information in the financial statements.

§ 227.202 Ongoing reporting requirements.

(a) An issuer that has offered and sold securities in reliance on Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)) and in accordance with Section 4A of the Securities Act (15 U.S.C. 77d-1) and this part must file with the Commission and post on the issuer's website an

annual report along with the financial statements of the issuer certified by the principal executive officer of the issuer to be true and complete in all material respects and a description of the financial condition of the issuer as described in § 227.201(s). If, however, an issuer has available financial statements that have either been reviewed or audited by a public accountant that is independent of the issuer, those financial statements must be provided and the certification by the principal executive officer will not be required. The annual report also must include the disclosure required by paragraphs (a), (b), (c), (d), (e), (f), (m), (p), (q), (r), and (x) of § 227.201. The report must be filed in accordance with the requirements of § 227.203 and Form C (§ 239.900 of this chapter) and no later than 120 days after the end of the fiscal year covered by the report.

Instruction 1 to paragraph (a). Instructions (3), (8), (9), (10), and (11) to paragraph (t) of § 227.201 shall apply for purposes of this section.

Instruction 2 to paragraph (a). An issuer providing financial statements that are not audited or reviewed must have its principal executive officer provide the following certification:

I, [identify the certifying individual], certify that the financial statements of [identify the issuer] included in this Form are true and complete in all material respects.

[Signature and title]. (b) An issuer must continue to comply with the ongoing reporting requirements until one of the following occurs:

(1) The issuer is required to file reports under Section 13(a) or Section 15(d) of the Exchange Act (15 U.S.C. 78m(a) or 78o(d));

(2) The issuer has filed, since its most recent sale of securities pursuant to this part, at least one annual report pursuant to this section and has fewer than 300 holders of record;

(3) The issuer has filed, since its most recent sale of securities pursuant to this part, the annual reports required pursuant to this section for at least the three most recent years and has total assets that do not exceed $10,000,000;

(4) The issuer or another party repurchases all of the securities issued in reliance on Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)), including any payment in full of debt securities or any complete redemption of redeemable securities; or

(5) The issuer liquidates or dissolves its business in accordance with state law.

§ 227.203 Filing requirements and form.

(a) Form C – Offering Statement and Amendments (§ 239.900 of this chapter).

(1) *Offering Statement.* An issuer offering or selling securities in reliance on Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)) and in accordance with Section 4A of the Securities Act (15 U.S.C. 77d-1) and this part must file with the Commission and provide to investors and the relevant intermediary a Form C: Offering Statement (Form C) (§ 239.900 of this chapter) prior to the commencement of the offering of securities. The Form C must include the information required by § 227.201.

(2) *Amendments to Offering Statement.* An issuer must file with the Commission and provide to investors and the relevant intermediary an amendment to the offering statement filed on Form C (§ 239.900 of this chapter) to disclose any material changes, additions or updates to information that it provides to investors through the intermediary's platform, for any offering that has not yet been completed or terminated. The amendment must be filed on Form C: Amendment (Form C/A) (§ 239.900 of this chapter), and if the amendment reflects material changes, additions or updates, the issuer shall check the box indicating that investors must reconfirm an investment commitment within five business days or the investor's commitment will be considered cancelled.

(3) *Progress Updates.*

(i) An issuer must file with the Commission and provide to investors and the relevant intermediary a Form C: Progress Update (Form C-U) (§ 239.900 of this chapter) to disclose its progress in meeting the target offering amount no later than five business days after each of the dates when the issuer reaches 50 percent and 100 percent of the target offering amount.

(ii) If the issuer will accept proceeds in excess of the target offering amount, the issuer must file with the Commission and provide to investors and the relevant intermediary, no later than five business days after the offering deadline, a final Form C-U (§ 239.900 of this chapter) to disclose the total amount of securities sold in the offering.

(iii) The requirements of paragraphs (a)(3)(i) and (ii) of this section shall not apply to an issuer if the relevant intermediary makes publicly available on the intermediary's platform frequent updates regarding the progress of the issuer in meeting the target offering amount; however, the issuer must still file a Form C-U (§ 239.900 of this chapter) to disclose the total amount of securities sold in the offering no later than five business days after the offering deadline.

Instruction to paragraph (a)(3). If multiple Forms C-U (§ 239.900 of this chapter) are triggered within the same five business day period, the issuer may consolidate such progress updates into one Form C-U, so long as the Form C-U discloses the most recent threshold that was met and the Form C-U is filed with the Commission and provided to investors and the relevant intermediary by the day on which the first progress update is due.

Instruction 1 to paragraph (a). An issuer would satisfy the requirement to provide to the relevant intermediary the information required by this paragraph (a) if it provides to the relevant intermediary a copy of the disclosures filed with the Commission.

Instruction 2 to paragraph (a). An issuer would satisfy the requirement to provide to investors the information required by this paragraph (a) if the issuer refers investors to the information on the intermediary's platform by means of a posting on the issuer's website or by e-mail.

(b) Form C: Annual Report and Termination of Reporting (§ 239.900 of this chapter).

(1) *Annual Reports*. An issuer that has sold securities in reliance on Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)) and in accordance with Section 4A of the Securities Act (15 U.S.C. 77d-1) and this part must file an annual report on Form C: Annual Report (Form C-AR) (§ 239.900 of this chapter) with the Commission no later than 120 days after the end of the fiscal year covered by the report. The annual report shall include the information required by § 227.202(a).

(2) *Amendments to Annual Report*. An issuer must file with the Commission an amendment to the annual report filed on Form C: Annual Report (Form C-AR) (§ 239.900 of this chapter) to make a material change to the previously filed annual report as soon as practicable after discovery of the need for the material change. The amendment must be filed on Form C: Amendment to Annual Report (Form C-AR/A) (§ 239.900 of this chapter).

(3) *Termination of Reporting*. An issuer eligible to terminate its obligation to file annual reports with the Commission pursuant to § 227.202(b) must file with the Commission, within five business days from the date on which the issuer becomes eligible to terminate its reporting obligation, Form C: Termination of Reporting (Form C-TR) (§ 239.900 of this chapter) to advise investors that the issuer will cease reporting pursuant to this part.

§ 227.204 Advertising.

(a) An issuer may not, directly or indirectly, advertise the terms of an offering made in reliance on Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)), except for notices that meet the requirements of paragraph (b) of this section.

Instruction to § 227.204(a). For purposes of this paragraph (a), *issuer* includes persons acting on behalf of the issuer.

(b) A notice may advertise any of the terms of an issuer's offering made in reliance on Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)) if it directs investors to the intermediary's platform and includes no more than the following information:

(1) A statement that the issuer is conducting an offering pursuant to Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)), the name of the intermediary through which the offering is being conducted and a link directing the potential investor to the intermediary's platform;

(2) The terms of the offering; and

(3) Factual information about the legal identity and business location of the issuer, limited to the name of the issuer of the security, the address, phone number and website of the issuer, the e-mail address of a representative of the issuer and a brief description of the business of the issuer.

(c) Notwithstanding the prohibition on advertising any of the terms of the offering, an issuer, and persons acting on behalf of the issuer, may communicate with investors and potential investors about the terms of the offering through communication channels provided by the intermediary on the intermediary's platform, provided that an issuer identifies itself as the issuer in all communications. Persons acting on behalf of the issuer must identify their affiliation with the issuer in all communications on the intermediary's platform.

Instruction to § 227.204. For purposes of this section, *terms of the offering* means the amount of

securities offered, the nature of the securities, the price of the securities and the closing date of the offering period.

§ 227.205 Promoter compensation.

(a) An issuer, or person acting on behalf of the issuer, shall be permitted to compensate or commit to compensate, directly or indirectly, any person to promote the issuer's offerings made in reliance on Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)) through communication channels provided by an intermediary on the intermediary's platform, but only if the issuer or person acting on behalf of the issuer, takes reasonable steps to ensure that the person promoting the offering clearly discloses the receipt, past or prospective, of such compensation with any such communication.

Instruction to paragraph (a). The disclosure required by this paragraph is required, with each communication, for persons engaging in promotional activities on behalf of the issuer through the communication channels provided by the intermediary, regardless of whether or not the compensation they receive is specifically for the promotional activities. This includes persons hired specifically to promote the offering as well as to persons who are otherwise employed by the issuer or who undertake promotional activities on behalf of the issuer.

(b) Other than as set forth in paragraph (a) of this section, an issuer or person acting on behalf of the issuer shall not compensate or commit to compensate, directly or indirectly, any person to promote the issuer's offerings made in reliance on Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)), unless such promotion is limited to notices permitted by, and in compliance with, § 227.204.

SUBPART C – Requirements for Intermediaries

§ 227.300 Intermediaries.

(a) Requirements. A person acting as an intermediary in a transaction involving the offer or sale of securities in reliance on Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)) must:

(1) Be registered with the Commission as a broker under Section 15(b) of the Exchange Act (15 U.S.C. 78*o*(b)) or as a funding portal in accordance with the requirements of § 227.400; and

(2) Be a member a national securities association registered under Section 15A of the Exchange Act (15 U.S.C. 78*o*-3).

(b) Financial Interests. Any director, officer or partner of an intermediary, or any person occupying a similar status or performing a similar function, may not have a financial interest in an issuer that is offering or selling securities in reliance on Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)) through the intermediary's platform, or receive a financial interest in an issuer as compensation for the services provided to or for the benefit of the issuer in connection with the offer or sale of such securities. An intermediary may not have a financial interest in an issuer that is offering or selling securities in reliance on Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)) through the intermediary's platform unless:

(1) the intermediary receives the financial interest from the issuer as compensation for the services provided to, or for the benefit of, the issuer in connection with the offer or sale of the securities being offered or sold in reliance on Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)) through the intermediary's platform; and

(2) the financial interest consists of securities of the same class and having the same terms, conditions and rights as the securities being offered or sold in reliance on Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)) through the intermediary's platform. For purposes of this paragraph, a *financial interest in an issuer* means a direct or indirect ownership of, or economic interest in, any class of the issuer's securities.

(c) Definitions. For purposes of this part:

(1) *Associated person of a funding portal* or *person associated with a funding portal* means any partner, officer, director or manager of a funding portal (or any person occupying a similar status or performing similar functions), any person directly or indirectly controlling or controlled by such funding portal, or any employee of a funding portal, except that any person associated with a funding portal whose functions are solely clerical or ministerial shall not be included in the meaning of such term for purposes of Section 15(b) of the Exchange Act (15 U.S.C. 78*o*(b)) (other than paragraphs (4) and (6) of Section 15(b) of the Exchange Act).

(2) *Funding portal* means a broker acting as an intermediary in a transaction involving the offer or sale of securities in reliance on Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)), that does not:

(i) Offer investment advice or recommendations;

(ii) Solicit purchases, sales or offers to buy the securities displayed on its platform;

(iii) Compensate employees, agents, or other persons for such solicitation or based on the sale of securities displayed or referenced on its platform; or

(iv) Hold, manage, possess, or otherwise handle investor funds or securities.

(3) *Intermediary* means a broker registered under Section 15(b) of the Exchange Act (15 U.S.C. 78*o*(b)) or a funding portal registered under § 227.400 and includes, where relevant, an associated person of the registered broker or registered funding portal.

(4) *Platform* means a program or application accessible via the Internet or other similar electronic communication medium through which a registered broker or a registered funding portal acts as an intermediary in a transaction involving the offer or sale of securities in reliance on Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)).

Instruction to paragraph (c)(4). An intermediary through which a crowdfunding transaction is conducted may engage in back office or other administrative functions other than on the intermediary's platform.

§ 227.301 Measures to reduce risk of fraud.

An intermediary in a transaction involving the offer or sale of securities in reliance on Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)) must:

(a) Have a reasonable basis for believing that an issuer seeking to offer and sell securities in reliance on Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)) through the intermediary's platform complies with the requirements in Section 4A(b) of the Act (15 U.S.C. 77d-1(b)) and the related requirements in this part. In satisfying this requirement, an intermediary may rely on the representations of the issuer concerning compliance with these requirements unless the intermediary has reason to question the reliability of those representations;

(b) Have a reasonable basis for believing that the issuer has established means to keep accurate records of the holders of the securities it would offer and sell through the intermediary's platform, provided that an intermediary may rely on the representations of the issuer concerning its means of recordkeeping unless the intermediary has reason to question the reliability of those

representations. An intermediary will be deemed to have satisfied this requirement if the issuer has engaged the services of a transfer agent that is registered under Section 17A of the Exchange Act (15 U.S.C. 78q-1(c)).

(c) Deny access to its platform to an issuer if the intermediary:

(1) Has a reasonable basis for believing that the issuer or any of its officers, directors (or any person occupying a similar status or performing a similar function) or beneficial owners of 20 percent or more of the issuer's outstanding voting equity securities, calculated on the basis of voting power, is subject to a disqualification under § 227.503. In satisfying this requirement, an intermediary must, at a minimum, conduct a background and securities enforcement regulatory history check on each issuer whose securities are to be offered by the intermediary and on each officer, director or beneficial owner of 20 percent or more of the issuer's outstanding voting equity securities, calculated on the basis of voting power.

(2) Has a reasonable basis for believing that the issuer or the offering presents the potential for fraud or otherwise raises concerns about investor protection. In satisfying this requirement, an intermediary must deny access if it reasonably believes that it is unable to adequately or effectively assess the risk of fraud of the issuer or its potential offering. In addition, if an intermediary becomes aware of information after it has granted access that causes it to reasonably believe that the issuer or the offering presents the potential for fraud or otherwise raises concerns about investor protection, the intermediary must promptly remove the offering from its platform, cancel the offering, and return (or, for funding portals, direct the return of) any funds that have been committed by investors in the offering.

§ 227.302 Account opening.

(a) Accounts and Electronic Delivery.

(1) No intermediary or associated person of an intermediary may accept an investment commitment in a transaction involving the offer or sale of securities in reliance on Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)) until the investor has opened an account with the intermediary and the intermediary has obtained from the investor consent to electronic delivery of materials.

(2) An intermediary must provide all information that is required to be provided by the intermediary under Subpart C (§§ 227.300 through 305), including, but not limited to, educational materials, notices and confirmations, through electronic means. Unless otherwise indicated in the relevant rule of Subpart C, in satisfying this requirement, an intermediary must provide the information through an electronic message that contains the information, through an electronic message that includes a specific link to the information as posted on intermediary's platform, or through an electronic message that provides notice of what the information is and that it is located on the intermediary's platform or on the issuer's website. Electronic messages include, but are not limited to, e-mail, social media messages, instant messages or other electronic media messages.

(b) Educational Materials. (1) In connection with establishing an account for an investor, an intermediary must deliver educational materials to such investor that explain in plain language and are otherwise designed to communicate effectively and accurately:

(i) The process for the offer, purchase and issuance of securities through the intermediary and the risks associated with purchasing securities offered and sold in reliance on Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6));

(ii) The types of securities offered and sold in reliance on Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)) available for purchase on the intermediary's platform and the risks

associated with each type of security, including the risk of having limited voting power as a result of dilution;

(iii) The restrictions on the resale of a security offered and sold in reliance on Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6));

(iv) The types of information that an issuer is required to provide under § 227.202, the frequency of the delivery of that information and the possibility that those obligations may terminate in the future;

(v) The limitations on the amounts an investor may invest pursuant to § 227.100(a)(2);

(vi) The limitations on an investor's right to cancel an investment commitment and the circumstances in which an investment commitment may be cancelled by the issuer;

(vii) The need for the investor to consider whether investing in a security offered and sold in reliance on Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)) is appropriate for that investor;

(viii) That following completion of an offering conducted through the intermediary, there may or may not be any ongoing relationship between the issuer and intermediary; and

(ix) That under certain circumstances an issuer may cease to publish annual reports and, therefore, an investor may not continually have current financial information about the issuer.

(2) An intermediary must make the most current version of its educational material available on its platform at all times and, if at any time, the intermediary makes a material revision to its educational materials, it must make the revised educational materials available to all investors before accepting any additional investment commitments or effecting any further transactions in securities offered and sold in reliance on Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)).

(c) Promoters. In connection with establishing an account for an investor, an intermediary must inform the investor that any person who promotes an issuer's offering for compensation, whether past or prospective, or who is a founder or an employee of an issuer that engages in promotional activities on behalf of the issuer on the intermediary's platform, must clearly disclose in all communications on the intermediary's platform, respectively, the receipt of the compensation and that he or she is engaging in promotional activities on behalf of the issuer.

(d) Compensation Disclosure. When establishing an account for an investor, an intermediary must clearly disclose the manner in which the intermediary is compensated in connection with offerings and sales of securities in reliance on Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)).

§ 227.303 Requirements with respect to transactions.

(a) Issuer Information. An intermediary in a transaction involving the offer or sale of securities in reliance on Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)) must make available to the Commission and to investors any information required to be provided by the issuer of the securities under §§ 227.201 and 203(a).

(1) This information must be made publicly available on the intermediary's platform, in a manner that reasonably permits a person accessing the platform to save, download, or otherwise store the information;

(2) This information must be made publicly available on the intermediary's platform for a minimum of 21 days before any securities are sold in the offering, during which time the intermediary may accept investment commitments;

(3) This information, including any additional information provided by the issuer, must remain publicly available on the intermediary's platform until the offer and sale of securities in

reliance on Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)) is completed or cancelled; and

(4) An intermediary may not require any person to establish an account with the intermediary to access this information.

(b) Investor Qualification. Each time before accepting any investment commitment (including any additional investment commitment from the same person), an intermediary must:

(1) Have a reasonable basis for believing that the investor satisfies the investment limitations established by Section 4(a)(6)(B) of the Act (15 U.S.C. 77d(a)(6)(B)) and this part. An intermediary may rely on an investor's representations concerning compliance with the investment limitation requirements concerning the investor's annual income, net worth, and the amount of the investor's other investments made pursuant to Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)) unless the intermediary has reason to question the reliability of the representation.

(2) Obtain from the investor:

(i) A representation that the investor has reviewed the intermediary's educational materials delivered pursuant to § 227.302(b), understands that the entire amount of his or her investment may be lost, and is in a financial condition to bear the loss of the investment; and

(ii) A questionnaire completed by the investor demonstrating the investor's understanding that:

(A) There are restrictions on the investor's ability to cancel an investment commitment and obtain a return of his or her investment;

(B) It may be difficult for the investor to resell securities acquired in reliance on Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)); and

(C) Investing in securities offered and sold in reliance on Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)) involves risk, and the investor should not invest any funds in an offering made in reliance on Section 4(a)(6) of the Securities Act unless he or she can afford to lose the entire amount of his or her investment.

(c) Communication Channels. An intermediary must provide on its platform communication channels by which persons can communicate with one another and with representatives of the issuer about offerings made available on the intermediary's platform, provided:

(1) If the intermediary is a funding portal, it does not participate in these communications other than to establish guidelines for communication and remove abusive or potentially fraudulent communications;

(2) The intermediary permits public access to view the discussions made in the communication channels;

(3) The intermediary restricts posting of comments in the communication channels to those persons who have opened an account with the intermediary on its platform; and

(4) The intermediary requires that any person posting a comment in the communication channels clearly and prominently disclose with each posting whether he or she is a founder or an employee of an issuer engaging in promotional activities on behalf of the issuer, or is otherwise compensated, whether in the past or prospectively, to promote the issuer's offering.

(d) Notice of Investment Commitment. An intermediary must promptly, upon receipt of an investment commitment from an investor, give or send to the investor a notification disclosing:

(1) The dollar amount of the investment commitment;

(2) The price of the securities, if known;

(3) The name of the issuer; and

(4) The date and time by which the investor may cancel the investment commitment.

(e) Maintenance and Transmission of Funds.

(1) An intermediary that is a registered broker must comply with the requirements of 17 CFR 240.15c2-4.

(2) An intermediary that is a funding portal must direct investors to transmit the money or other consideration directly to a qualified third party that has agreed in writing to hold the funds for the benefit of, and to promptly transmit or return the funds to, the persons entitled thereto in accordance with paragraph (e)(3) of this section. For purposes of this Subpart C (§§ 227.300 through 305), a qualified third party means a:

(i) Registered broker or dealer that carries customer or broker or dealer accounts and holds funds or securities for those persons; or

(ii) Bank or credit union (where such credit union is insured by National Credit Union Administration) that has agreed in writing either to hold the funds in escrow for the persons who have the beneficial interests therein and to transmit or return such funds directly to the persons entitled thereto when so directed by the funding portal as described in paragraph (e)(3) of this section, or to maintain a bank or credit union account (or accounts) for the exclusive benefit of investors and the issuer.

(3) A funding portal that is an intermediary in a transaction involving the offer or sale of securities in reliance on Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)) shall promptly direct the qualified third party to:

(i) Transmit funds from the qualified third party to the issuer when the aggregate amount of investment commitments from all investors is equal to or greater than the target amount of the

offering and the cancellation period as set forth in § 227.304 has elapsed, *provided that* in no event may the funding portal direct this transmission of funds earlier than 21 days after the date on which the intermediary makes publicly available on its platform the information required to be provided by the issuer under §§ 227.201 and 203(a);

(ii) Return funds to an investor when an investment commitment has been cancelled in accordance with § 227.304 (including for failure to obtain effective reconfirmation as required under § 227.304(c)); and

(iii) Return funds to investors when an issuer does not complete the offering.

(f) Confirmation of Transaction. (1) An intermediary must, at or before the completion of a transaction in a security in reliance on Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)), give or send to each investor a notification disclosing:

(i) The date of the transaction;

(ii) The type of security that the investor is purchasing;

(iii) The identity, price, and number of securities purchased by the investor, as well as the number of securities sold by the issuer in the transaction and the price(s) at which the securities were sold;

(iv) If a debt security, the interest rate and the yield to maturity calculated from the price paid and the maturity date;

(v) If a callable security, the first date that the security can be called by the issuer; and

(vi) The source, form and amount of any remuneration received or to be received by the intermediary in connection with the transaction, including any remuneration received or to be received by the intermediary from persons other than the issuer.

(2) An intermediary satisfying the requirements of paragraph (f)(1) of this section is exempt from the requirements of §240.10b-10 of this chapter with respect to a transaction in a security offered and sold in reliance on Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)).

§ 227.304 Completion of offerings, cancellations and reconfirmations.

(a) Generally. An investor may cancel an investment commitment for any reason until 48 hours prior to the deadline identified in the issuer's offering materials. During the 48 hours prior to such deadline, an investment commitment may not be cancelled except as provided in paragraph (c) of this section.

(b) Early Completion of Offering. If an issuer reaches the target offering amount prior to the deadline identified in its offering materials pursuant to § 227.201(g), the issuer may close the offering on a date earlier than the deadline identified in its offering materials pursuant to § 227.201(g), *provided that:*

(1) The offering remains open for a minimum of 21 days pursuant to § 227.303(a);

(2) The intermediary provides notice to any potential investors, and gives or sends notice to investors that have made investment commitments in the offering, of:

(i) The new, anticipated deadline of the offering;

(ii) The right of investors to cancel investment commitments for any reason until 48 hours prior to the new offering deadline; and

(iii) Whether the issuer will continue to accept investment commitments during the 48-hour period prior to the new offering deadline.

(3) The new offering deadline is scheduled for and occurs at least five business days after the notice required in paragraph (b)(2) of this section is provided; and

(4) At the time of the new offering deadline, the issuer continues to meet or exceed the target offering amount.

(c) Cancellations and Reconfirmations Based on Material Changes. (1) If there is a material change to the terms of an offering or to the information provided by the issuer, the intermediary must give or send to any investor who has made an investment commitment notice of the material change and that the investor's investment commitment will be cancelled unless the investor reconfirms his or her investment commitment within five business days of receipt of the notice. If the investor fails to reconfirm his or her investment within those five business days, the intermediary within five business days thereafter must:

(i) Give or send the investor a notification disclosing that the commitment was cancelled, the reason for the cancellation and the refund amount that the investor is expected to receive; and

(ii) Direct the refund of investor funds.

(2) If material changes to the offering or to the information provided by the issuer regarding the offering occur within five business days of the maximum number of days that an offering is to remain open, the offering must be extended to allow for a period of five business days for the investor to reconfirm his or her investment.

(d) Return of Funds If Offering Is Not Completed. If an issuer does not complete an offering, an intermediary must within five business days:

(1) Give or send each investor a notification of the cancellation, disclosing the reason for the cancellation, and the refund amount that the investor is expected to receive;

(2) Direct the refund of investor funds; and

(3) Prevent investors from making investment commitments with respect to that offering on its platform.

§ 227.305 Payments to third parties.

(a) Prohibition on Payments for Personally Identifiable Information. An intermediary may not compensate any person for providing the intermediary with the personally identifiable information of any investor or potential investor in securities offered and sold in reliance on Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)).

(b) For purposes of this rule, personally identifiable information means information that can be used to distinguish or trace an individual's identity, either alone or when combined with other personal or identifying information that is linked or linkable to a specific individual.

SUBPART D – Funding Portal Regulation

§227.400 Registration of funding portals.

(a) Registration. A funding portal must register with the Commission, by filing a complete Form Funding Portal (§ 249.2000 of this chapter) in accordance with the instructions on the form, and become a member of a national securities association registered under Section 15A of the Exchange Act (15 U.S.C. 78*o*-3). The registration will be effective the later of:

(1) 30 calendar days after the date that the registration is received by the Commission; or

(2) The date the funding portal is approved for membership by a national securities association registered under Section 15A of the Exchange Act (15 U.S.C. 78*o*-3).

(b) Amendments to Registration. A funding portal must file an amendment to Form Funding Portal (§ 249.2000 of this chapter) within 30 days of any of the information previously submitted on Form Funding Portal becoming inaccurate for any reason.

(c) Successor Registration.

(1) If a funding portal succeeds to and continues the business of a registered funding portal, the registration of the predecessor will remain effective as the registration of the successor

if the successor, within 30 days after such succession, files a registration on Form Funding Portal (§ 249.2000 of this chapter) and the predecessor files a withdrawal on Form Funding Portal; *provided, however*, that the registration of the predecessor funding portal will be deemed withdrawn 45 days after registration on Form Funding Portal is filed by the successor.

(2) Notwithstanding paragraph (c)(1) of this section, if a funding portal succeeds to and continues the business of a registered funding portal and the succession is based solely on a change of the predecessor's date or state of incorporation, form of organization, or composition of a partnership, the successor may, within 30 days after the succession, amend the registration of the predecessor on Form Funding Portal (§ 249.2000 of this chapter) to reflect these changes.

(d) Withdrawal. A funding portal must promptly file a withdrawal of registration on Form Funding Portal (§ 249.2000 of this chapter) in accordance with the instructions on the form upon ceasing to operate as a funding portal. Withdrawal will be effective on the later of 30 days after receipt by the Commission (after the funding portal is no longer operational), or within such longer period of time as to which the funding portal consents or which the Commission by order may determine as necessary or appropriate in the public interest or for the protection of investors.

(e) Applications and Reports. The applications and reports provided for in this section shall be considered filed when a complete Form Funding Portal (§ 249.2000 of this chapter) is submitted with the Commission. Duplicate originals of the applications and reports provided for in this section must be filed with surveillance personnel designated by any registered national securities association of which the funding portal is a member.

(f) Nonresident Funding Portals. Registration pursuant to this section by a nonresident funding portal shall be conditioned upon there being an information sharing arrangement in place between the Commission and the competent regulator in the jurisdiction under the laws of which

the nonresident funding portal is organized or where it has its principal place of business, that is applicable to the nonresident funding portal.

(1) *Definition.* For purposes of this section, the term *nonresident funding portal* shall mean a funding portal incorporated in or organized under the laws of a jurisdiction outside of the United States or its territories, or having its principal place of business in any place not in the United States or its territories.

(2) *Power of Attorney*.

(i) Each nonresident funding portal registered or applying for registration pursuant to this section shall obtain a written consent and power of attorney appointing an agent in the United States, other than the Commission or a Commission member, official or employee, upon whom may be served any process, pleadings or other papers in any action under the federal securities laws. This consent and power of attorney must be signed by the nonresident funding portal and the named agent(s) for service of process.

(ii) Each nonresident funding portal registered or applying for registration pursuant to this section shall, at the time of filing its application on Form Funding Portal (§ 249.2000 of this chapter), furnish to the Commission the name and address of its United States agent for service of process on Schedule C to the Form.

(iii) Any change of a nonresident funding portal's agent for service of process and any change of name or address of a nonresident funding portal's existing agent for service of process shall be communicated promptly to the Commission through amendment of the Schedule C to Form Funding Portal (§ 249.2000 of this chapter).

(iv) Each nonresident funding portal must promptly appoint a successor agent for service of process if the nonresident funding portal discharges its identified agent for service of process or

if its agent for service of process is unwilling or unable to accept service on behalf of the nonresident funding portal.

(v) Each nonresident funding portal must maintain, as part of its books and records, the written consent and power of attorney identified in paragraph (f)(2)(i) of this section for at least three years after the agreement is terminated.

(3) *Access to Books and Records; Inspections and Examinations*.

(i) *Certification and Opinion of Counsel*. Any nonresident funding portal applying for registration pursuant to this section shall:

(A) Certify on Schedule C to Form Funding Portal (§ 249.2000 of this chapter) that the nonresident funding portal can, as a matter of law, and will provide the Commission and any registered national securities association of which it becomes a member with prompt access to the books and records of such nonresident funding portal and can, as a matter of law, and will submit to onsite inspection and examination by the Commission and any registered national securities association of which it becomes a member; and

(B) Provide an opinion of counsel that the nonresident funding portal can, as a matter of law, provide the Commission and any registered national securities association of which it becomes a member with prompt access to the books and records of such nonresident funding portal and can, as a matter of law, submit to onsite inspection and examination by the Commission and any registered national securities association of which it becomes a member.

(ii) *Amendments*. The nonresident funding portal shall re-certify, on Schedule C to Form Funding Portal (§ 249.2000 of this chapter), within 90 days after any changes in the legal or regulatory framework that would impact the nonresident funding portal's ability to provide, or the manner in which it provides, the Commission, or any registered national securities association of

which it is a member, with prompt access to its books and records or that would impact the Commission's or such registered national securities association's ability to inspect and examine the nonresident funding portal. The re-certification shall be accompanied by a revised opinion of counsel describing how, as a matter of law, the nonresident funding portal can continue to meet its obligations under paragraphs (f)(3)(i)(A) and (B) of this section.

§ 227.401 Exemption.

A funding portal that is registered with the Commission pursuant to § 227.400 is exempt from the broker registration requirements of Section 15(a)(1) of the Exchange Act (15 U.S.C. 78*o*(a)(1)) in connection with its activities as a funding portal.

§ 227.402 Conditional safe harbor.

(a) General. Under Section 3(a)(80) of the Exchange Act (15 U.S.C. 78c(a)(80)), a funding portal acting as an intermediary in a transaction involving the offer or sale of securities in reliance on Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)) may not: offer investment advice or recommendations; solicit purchases, sales, or offers to buy the securities offered or displayed on its platform or portal; compensate employees, agents, or other persons for such solicitation or based on the sale of securities displayed or referenced on its platform or portal; hold, manage, possess, or otherwise handle investor funds or securities; or engage in such other activities as the Commission, by rule, determines appropriate. This section is intended to provide clarity with respect to the ability of a funding portal to engage in certain activities, consistent with the prohibitions under Section 3(a)(80) of the Exchange Act. No presumption shall arise that a funding portal has violated the prohibitions under Section 3(a)(80) of the Exchange Act or this part by reason of the funding portal or its associated persons engaging in activities in connection with the offer or sale of securities in reliance on Section 4(a)(6) of the Securities Act that do not

meet the conditions specified in paragraph (b) of this section. The antifraud provisions and all other applicable provisions of the federal securities laws continue to apply to the activities described in paragraph (b) of this section.

(b) Permitted Activities. A funding portal may, consistent with the prohibitions under Section 3(a)(80) of the Exchange Act (15 U.S.C. 78c(a)(80)) and this part:

(1) Determine whether and under what terms to allow an issuer to offer and sell securities in reliance on Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)) through its platform; provided that a funding portal otherwise complies with this part;

(2) Apply objective criteria to highlight offerings on the funding portal's platform where:

(i) The criteria are reasonably designed to highlight a broad selection of issuers offering securities through the funding portal's platform, are applied consistently to all issuers and offerings and are clearly displayed on the funding portal's platform;

(ii) The criteria may include, among other things, the type of securities being offered (for example, common stock, preferred stock or debt securities); the geographic location of the issuer; the industry or business segment of the issuer; the number or amount of investment commitments made, progress in meeting the issuer's target offering amount or, if applicable, the maximum offering amount; and the minimum or maximum investment amount; provided that the funding portal may not highlight an issuer or offering based on the advisability of investing in the issuer or its offering; and

(iii) The funding portal does not receive special or additional compensations for highlighting one or more issuers or offerings on its platform;

(3) Provide search functions or other tools that investors can use to search, sort, or categorize the offerings available through the funding portal's platform according to objective criteria where;

(i) The criteria may include, among other things, the type of securities being offered (for example, common stock, preferred stock or debt securities); the geographic location of the issuer; the industry or business segment of the issuer; the number or amount of investment commitments made, progress in meeting the issuer's target offering amount or, if applicable, the maximum offering amount; and the minimum or maximum investment amount; and

(ii) The criteria may not include, among other things, the advisability of investing in the issuer or its offering, or an assessment of any characteristic of the issuer, its business plan, its key management or risks associated with an investment.

(4) Provide communication channels by which investors can communicate with one another and with representatives of the issuer through the funding portal's platform about offerings through the platform, so long as the funding portal (and its associated persons):

(i) Does not participate in these communications, other than to establish guidelines for communication and remove abusive or potentially fraudulent communications;

(ii) Permits public access to view the discussions made in the communication channels;

(iii) Restricts posting of comments in the communication channels to those persons who have opened an account on its platform; and

(iv) Requires that any person posting a comment in the communication channels clearly disclose with each posting whether he or she is a founder or an employee of an issuer engaging in promotional activities on behalf of the issuer, or is otherwise compensated, whether in the past or prospectively, to promote an issuer's offering;

(5) Advise an issuer about the structure or content of the issuer's offering, including assisting the issuer in preparing offering documentation;

(6) Compensate a third party for referring a person to the funding portal, so long as the third party does not provide the funding portal with personally identifiable information of any potential investor, and the compensation, other than that paid to a registered broker or dealer, is not based, directly or indirectly, on the purchase or sale of a security in reliance on Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)) offered on or through the funding portal's platform;

(7) Pay or offer to pay any compensation to a registered broker or dealer for services, including referrals pursuant to paragraph (b)(6) of this section, in connection with the offer or sale of securities by the funding portal in reliance on Section 4(a)(6) of the Act(15 U.S.C. 77d(a)(6)), provided that:

(i) Such services are provided pursuant to a written agreement between the funding portal and the registered broker or dealer;

(ii) Such services and compensation are permitted under this part; and

(iii) Such services and compensation comply with the rules of any registered national securities association of which the funding portal is a member;

(8) Receive any compensation from a registered broker or dealer for services provided by the funding portal in connection with the offer or sale of securities by the funding portal in reliance on Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)), provided that:

(i) Such services are provided pursuant to a written agreement between the funding portal and the registered broker or dealer;

(ii) Such compensation is permitted under this part; and

(iii) Such compensation complies with the rules of any registered national securities association of which the funding portal is a member;

(9) Advertise the existence of the funding portal and identify one or more issuers or offerings available on the portal on the basis of objective criteria, as long as:

(i) The criteria are reasonably designed to identify a broad selection of issuers offering securities through the funding portal's platform, and are applied consistently to all potential issuers and offerings;

(ii) The criteria may include, among other things, the type of securities being offered (for example, common stock, preferred stock or debt securities); the geographic location of the issuer; the industry or business segment of the issuer; the expressed interest by investors, as measured by number or amount of investment commitments made, progress in meeting the issuer's target offering amount or, if applicable, the maximum offering amount; and the minimum or maximum investment amount; and

(iii) The funding portal does not receive special or additional compensation for identifying the issuer or offering in this manner;

(10) Deny access to its platform to, or cancel an offering of an issuer, pursuant to § 227.301(c)(2), if the funding portal has a reasonable basis for believing that the issuer or the offering presents the potential for fraud or otherwise raises concerns about investor protection;

(11) Accept, on behalf of an issuer, an investment commitment for securities offered in reliance on Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)) by that issuer on the funding portal's platform;

(12) Direct investors where to transmit funds or remit payment in connection with the purchase of securities offered and sold in reliance on Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)); and

(13) Direct a qualified third party, as required by § 227.303(e), to release proceeds to an issuer upon completion of a crowdfunding offering or to return proceeds to investors in the event an investment commitment or an offering is cancelled.

§ 227.403 Compliance.

(a) Policies and procedures. A funding portal must implement written policies and procedures reasonably designed to achieve compliance with the federal securities laws and the rules and regulations thereunder relating to its business as a funding portal.

(b) Privacy. A funding portal must comply with the requirements of part 248 of this chapter as they apply to brokers.

(c) Inspections and examinations. A funding portal shall permit the examination and inspection of all of its business and business operations that relate to its activities as a funding portal, such as its premises, systems, platforms, and records by representatives of the Commission and of the registered national securities association of which it is a member.

§ 227.404 Records to be made and kept by funding portals.

(a) Generally. A funding portal shall make and preserve the following records for five years, the first two years in an easily accessible place:

(1) All records related to an investor who purchases or attempts to purchase securities through the funding portal;

(2) All records related to issuers who offer and sell or attempt to offer and sell securities through the funding portal and the control persons of such issuers;

(3) Records of all communications that occur on or through its platform;

(4) All records related to persons that use communication channels provided by a funding portal to promote an issuer's securities or communicate with potential investors;

(5) All records required to demonstrate compliance with the requirements of Subparts C (§§ 227.300 through 305) and D (§§ 227.400 through 404);

(6) All notices provided by such funding portal to issuers and investors generally through the funding portal's platform or otherwise, including, but not limited to, notices addressing hours of funding portal operations (if any), funding portal malfunctions, changes to funding portal procedures, maintenance of hardware and software, instructions pertaining to access to the funding portal and denials of, or limitations on, access to the funding portal;

(7) All written agreements (or copies thereof) entered into by such funding portal relating to its business as such;

(8) All daily, monthly and quarterly summaries of transactions effected through the funding portal, including:

(i) Issuers for which the target offering amount has been reached and funds distributed; and

(ii) Transaction volume, expressed in:

(A) Number of transactions;

(B) Number of securities involved in a transaction;

(C) Total amounts raised by, and distributed to, issuers; and

(D) Total dollar amounts raised across all issuers, expressed in U.S. dollars; and

(9) A log reflecting the progress of each issuer who offers or sells securities through the funding portal toward meeting the target offering amount.

(b) Organizational documents. A funding portal shall make and preserve during the operation of the funding portal and of any successor funding portal, all organizational documents relating to the funding portal, including but not limited to, partnership agreements, articles of incorporation or charter, minute books and stock certificate books (or other similar type documents).

(c) Format. The records required to be maintained and preserved pursuant to paragraph (a) of this section must be produced, reproduced, and maintained in the original, non-alterable format in which they were created or as permitted under § 240.17a-4(f) of this chapter.

(d) Third parties. The records required to be made and preserved pursuant to this section may be prepared or maintained by a third party on behalf of a funding portal. An agreement with a third party shall not relieve a funding portal from the responsibility to prepare and maintain records as specified in this rule. A funding portal must file with the registered national securities association of which it is a member, a written undertaking in a form acceptable to the registered national securities association, signed by a duly authorized person of the third party, stating in effect that such records are the property of the funding portal and will be surrendered promptly on request of the funding portal. The undertaking shall include the following provision:

> With respect to any books and records maintained or preserved on behalf of [name of funding portal], the undersigned hereby acknowledges that the books and records are the property of [name of funding portal], and hereby undertakes to permit examination of such books and records at any time, or from time to time, during business hours by representatives of the Securities and Exchange Commission and the registered national securities association of which the funding portal is a member, and to promptly furnish to the Commission, its representatives,

and the registered national securities association of which the funding portal is a member, a true, correct, complete and current hard copy of any, all, or any part of, such books and records.

(e) Review of records. All records of a funding portal are subject at any time, or from time to time, to reasonable periodic, special, or other examination by the representatives of the Commission and the registered national securities association of which a funding portal is a member. Every funding portal shall furnish promptly to the Commission, its representatives, and the registered national securities association of which the funding portal is a member true, correct, complete and current copies of such records of the funding portal that are requested by the representatives of the Commission and the registered national securities association.

(f) Financial recordkeeping and reporting of currency and foreign transactions. A funding portal that is subject to the requirements of the Currency and Foreign Transactions Reporting Act of 1970 (15 U.S.C. 5311 *et seq.*) shall comply with the reporting, recordkeeping and record retention requirements of 31 CFR chapter X. Where 31 CFR chapter X and §§ 227.404(a) and 404(b) require the same records or reports to be preserved for different periods of time, such records or reports shall be preserved for the longer period of time.

SUBPART E – Miscellaneous Provisions

§ 227.501 Restrictions on resales.

(a) Securities issued in a transaction exempt from registration pursuant to Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)) and in accordance with Section 4A of the Securities Act (15 U.S.C. 77d-1) and this part may not be transferred by any purchaser of such securities during the one-year period beginning when the securities were issued in a transaction exempt from

registration pursuant to Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)), unless such securities are transferred:

(1) To the issuer of the securities;

(2) To an accredited investor;

(3) As part of an offering registered with the Commission; or

(4) To a member of the family of the purchaser or the equivalent, to a trust controlled by the purchaser, to a trust created for the benefit of a member of the family of the purchaser or the equivalent, or in connection with the death or divorce of the purchaser or other similar circumstance.

(b) For purposes of this § 227.501, the term *accredited investor* shall mean any person who comes within any of the categories set forth in § 230.501(a) of this chapter, or who the seller reasonably believes comes within any of such categories, at the time of the sale of the securities to that person.

(c) For purposes of this section, the term *member of the family of the purchaser or the equivalent* includes a child, stepchild, grandchild, parent, stepparent, grandparent, spouse or spousal equivalent, sibling, mother-in-law, father-in-law, son-in-law, daughter-in-law, brother-in-law, or sister-in-law of the purchaser, and shall include adoptive relationships. For purposes of this paragraph (c), the term *spousal equivalent* means a cohabitant occupying a relationship generally equivalent to that of a spouse.

§ 227.502 Insignificant deviations from a term, condition or requirement of Regulation Crowdfunding.

(a) A failure to comply with a term, condition, or requirement of this part will not result in the loss of the exemption from the requirements of Section 5 of the Securities Act (15 U.S.C. 77e)

for any offer or sale to a particular individual or entity, if the issuer relying on the exemption shows:

(1) The failure to comply was insignificant with respect to the offering as a whole;

(2) The issuer made a good faith and reasonable attempt to comply with all applicable terms, conditions and requirements of this part; and

(3) The issuer did not know of such failure where the failure to comply with a term, condition or requirement of this part was the result of the failure of the intermediary to comply with the requirements of Section 4A(a) of the Securities Act (15 U.S.C. 77d-1(a)) and the related rules, or such failure by the intermediary occurred solely in offerings other than the issuer's offering.

(b) Paragraph (a) of this section shall not preclude the Commission from bringing an enforcement action seeking any appropriate relief for an issuer's failure to comply with all applicable terms, conditions and requirements of this part.

§ 227.503 Disqualification provisions.

(a) Disqualification events. No exemption under this Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)) shall be available for a sale of securities if the issuer; any predecessor of the issuer; any affiliated issuer; any director, officer, general partner or managing member of the issuer; any beneficial owner of 20 percent or more of the issuer's outstanding voting equity securities, calculated on the basis of voting power; any promoter connected with the issuer in any capacity at the time of such sale; any person that has been or will be paid (directly or indirectly) remuneration for solicitation of purchasers in connection with such sale of securities; or any general partner, director, officer or managing member of any such solicitor:

(1) Has been convicted, within 10 years before the filing of the offering statement (or five years, in the case of issuers, their predecessors and affiliated issuers), of any felony or misdemeanor:

(i) In connection with the purchase or sale of any security;

(ii) Involving the making of any false filing with the Commission; or

(iii) Arising out of the conduct of the business of an underwriter, broker, dealer, municipal securities dealer, investment adviser, funding portal or paid solicitor of purchasers of securities;

(2) Is subject to any order, judgment or decree of any court of competent jurisdiction, entered within five years before the filing of the information required by Section 4A(b) of the Securities Act (15 U.S.C. 77d-1(b)) that, at the time of such filing, restrains or enjoins such person from engaging or continuing to engage in any conduct or practice:

(i) In connection with the purchase or sale of any security;

(ii) Involving the making of any false filing with the Commission; or

(iii) Arising out of the conduct of the business of an underwriter, broker, dealer, municipal securities dealer, investment adviser, funding portal or paid solicitor of purchasers of securities;

(3) Is subject to a final order of a state securities commission (or an agency or officer of a state performing like functions); a state authority that supervises or examines banks, savings associations or credit unions; a state insurance commission (or an agency or officer of a state performing like functions); an appropriate federal banking agency; the U.S. Commodity Futures Trading Commission; or the National Credit Union Administration that:

(i) At the time of the filing of the information required by Section 4A(b) of the Securities Act (15 U.S.C. 77d-1(b)), bars the person from:

(A) Association with an entity regulated by such commission, authority, agency or officer;

(B) Engaging in the business of securities, insurance or banking; or

(C) Engaging in savings association or credit union activities; or

(ii) Constitutes a final order based on a violation of any law or regulation that prohibits fraudulent, manipulative or deceptive conduct entered within ten years before such filing of the offering statement;

Instruction to paragraph (a)(3). Final order shall mean a written directive or declaratory statement issued by a federal or state agency, described in § 227.503(a)(3), under applicable statutory authority that provides for notice and an opportunity for hearing, which constitutes a final disposition or action by that federal or state agency.

(4) Is subject to an order of the Commission entered pursuant to Section 15(b) or 15B(c) of the Exchange Act (15 U.S.C. 78*o*(b) or 78*o*-4(c)) or Section 203(e) or (f) of the Investment Advisers Act of 1940 (15 U.S.C. 80b-3(e) or (f)) that, at the time of the filing of the information required by Section 4A(b) of the Securities Act (15 U.S.C. 77d-1(b)):

(i) Suspends or revokes such person's registration as a broker, dealer, municipal securities dealer, investment adviser or funding portal;

(ii) Places limitations on the activities, functions or operations of such person; or

(iii) Bars such person from being associated with any entity or from participating in the offering of any penny stock;

(5) Is subject to any order of the Commission entered within five years before the filing of the information required by Section 4A(b) of the Securities Act (15 U.S.C. 77d-1(b)) that, at the time of such filing, orders the person to cease and desist from committing or causing a violation or future violation of:

(i) Any scienter-based anti-fraud provision of the federal securities laws, including without limitation Section 17(a)(1) of the Securities Act (15 U.S.C. 77q(a)(1)), Section 10(b) of the Exchange Act (15 U.S.C. 78j(b)) and 17 CFR 240.10b-5, Section 15(c)(1) of the Exchange Act (15 U.S.C. 78o(c)(1)) and Section 206(1) of the Investment Advisers Act of 1940 (15 U.S.C. 80b-6(1)) or any other rule or regulation thereunder; or

(ii) Section 5 of the Securities Act (15 U.S.C. 77e);

(6) Is suspended or expelled from membership in, or suspended or barred from association with a member of, a registered national securities exchange or a registered national or affiliated securities association for any act or omission to act constituting conduct inconsistent with just and equitable principles of trade;

(7) Has filed (as a registrant or issuer), or was or was named as an underwriter in, any registration statement or Regulation A (17 CFR 230.251 *et seq*.) offering statement filed with the Commission that, within five years before the filing of the information required by Section 4A(b) of the Securities Act (15 U.S.C. 77d-1(b)), was the subject of a refusal order, stop order, or order suspending the Regulation A exemption, or is, at the time of such filing, the subject of an investigation or proceeding to determine whether a stop order or suspension order should be issued; or

(8) Is subject to a United States Postal Service false representation order entered within five years before the filing of the information required by Section 4A(b) of the Securities Act (15 U.S.C. 77d-1(b)), or is, at the time of such filing, subject to a temporary restraining order or preliminary injunction with respect to conduct alleged by the United States Postal Service to constitute a scheme or device for obtaining money or property through the mail by means of false representations.

(b) Transition, waivers, reasonable care exception. Paragraph (a) of this section shall not apply:

(1) With respect to any conviction, order, judgment, decree, suspension, expulsion or bar that occurred or was issued before [INSERT DATE 180 DAYS AFTER PUBLICATION IN THE FEDERAL REGISTER];

(2) Upon a showing of good cause and without prejudice to any other action by the Commission, if the Commission determines that it is not necessary under the circumstances that an exemption be denied;

(3) If, before the filing of the information required by Section 4A(b) of the Securities Act (15 U.S.C. 77d-1(b)), the court or regulatory authority that entered the relevant order, judgment or decree advises in writing (whether contained in the relevant judgment, order or decree or separately to the Commission or its staff) that disqualification under paragraph (a) of this section should not arise as a consequence of such order, judgment or decree; or

(4) If the issuer establishes that it did not know and, in the exercise of reasonable care, could not have known that a disqualification existed under paragraph (a) of this section.

Instruction to paragraph (b)(4). An issuer will not be able to establish that it has exercised reasonable care unless it has made, in light of the circumstances, factual inquiry into whether any disqualifications exist. The nature and scope of the factual inquiry will vary based on the facts and circumstances concerning, among other things, the issuer and the other offering participants.

(c) Affiliated issuers. For purposes of paragraph (a) of this section, events relating to any affiliated issuer that occurred before the affiliation arose will be not considered disqualifying if the affiliated entity is not:

(1) In control of the issuer; or

(2) Under common control with the issuer by a third party that was in control of the affiliated entity at the time of such events.

(d) Intermediaries. A person that is subject to a statutory disqualification as defined in Section 3(a)(39) of the Exchange Act (15 U.S.C. 78c(a)(39)) may not act as, or be an associated person of, an intermediary in a transaction involving the offer or sale of securities in reliance on Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)) unless so permitted pursuant to Commission rule or order.

Instruction to paragraph (d). § 240.17f-2 of this chapter generally requires the fingerprinting of every person who is a partner, director, officer or employee of a broker, subject to certain exceptions.

PART 232 – REGULATION S-T – GENERAL RULES AND REGULATIONS FOR ELECTRONIC FILINGS

4. The authority citation for part 232 continues to read, in part, as follows:

Authority: 15 U.S.C. 77c, 77f, 77g, 77h, 77j, 77s(a), 77z-3, 77sss(a), 78c(b), 781, 78m, 78n, 78o(d), 78w(a), 78ll, 80a-6(c), 80a-8, 80a-29, 80a-30, 80a-37, 7201 et seq.; and 18 U.S.C. 1350, unless otherwise noted.

* * * * *

5. Amend §232.101 by:

a. In paragraph (a)(1)(xvii) removing “and” at the end of the paragraph; and

b. In paragraph (a)(1)(xviii) removing the period at the end of the paragraph and adding in its place “; and”; and

c. Adding paragraphs (a)(1)(xix) and (a)(1)(xx).

The addition reads as follows:

§ 232.101 Mandated electronic submissions and exceptions.

(a) * * *

(1) * * *

(xix) Form C (§239.900 of this chapter). Exhibits to Form C (§239.900 of this chapter) may be filed on EDGAR as PDF documents in the format required by the EDGAR Filer Manual, as defined in Rule 11 of Regulation S-T (§232.11 of this chapter). Notwithstanding Rule 104 of Regulation S-T (§232.104 of this chapter), the PDF documents filed under this paragraph will be considered as officially filed with the Commission; and

(xx) Form Funding Portal (§249.2000 of this chapter). Exhibits and attachments to Form Funding Portal (§249.2000 of this chapter) may be filed on EDGAR as PDF documents in the format required by the EDGAR Filer Manual, as defined in Rule 11 of Regulation S-T (§232.11 of this chapter). Notwithstanding Rule 104 of Regulation S-T (§232.104 of this chapter), the PDF documents filed under this paragraph will be considered as officially filed with the Commission.

* * * * *

PART 239 – FORMS PRESCRIBED UNDER THE SECURITIES ACT OF 1933

6. The authority citation for part 239 continues to read, in part, as follows:

Authority: 15 U.S.C. 77c, 77f, 77g, 77h, 77j, 77s, 77z-2, 77z-3, 77sss, 78c, 78l, 78m, 78n, 78o(d), 78o-7 note, 78u-5, 78w(a), 78ll, 78mm, 80a-2(a), 80a-3, 80a-8, 80a-9, 80a-10, 80a-13, 80a-24, 80a-26, 80a-29, 80a-30, and 80a-37, unless otherwise noted.

* * * * *

7. Add § 239.900 to read as follows:

§ 239.900 Form C.

This form shall be used for filings under Regulation Crowdfunding (§§ 227.100 *et seq.* of this chapter).

Note: The text of Form C will not appear in the Code of Federal Regulations.

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM C

UNDER THE SECURITIES ACT OF 1933

(Mark one.)

□ **Form C: Offering Statement**
□ **Form C-U: Progress Update:** _____
□ **Form C/A: Amendment to Offering Statement:** _____
  □ **Check box if Amendment is material and investors must reconfirm within five business days.**
□ **Form C-AR: Annual Report**
□ **Form C-AR/A: Amendment to Annual Report**
□ **Form C-TR: Termination of Reporting**

Name of issuer: _____
Legal status of issuer:
  Form: _____
  Jurisdiction of Incorporation/Organization: _____
  Date of organization): _____
Physical address of issuer: _____
Website of issuer: _____

Name of intermediary through which the offering will be conducted: _____
CIK number of intermediary: _____
SEC file number of intermediary: _____
CRD number, if applicable, of intermediary: _____

Amount of compensation to be paid to the intermediary, whether as a dollar amount or a percentage of the offering amount, or a good faith estimate if the exact amount is not available at the time of the filing, for conducting the offering, including the amount of referral and any other fees associated with the offering:
_____

Any other direct or indirect interest in the issuer held by the intermediary, or any arrangement for the intermediary to acquire such an interest:
_____

Type of security offered: _____
Target number of securities to be offered: _____
Price (or method for determining price): _____
Target offering amount: _____
Oversubscriptions accepted: □ Yes □ No

If yes, disclose how oversubscriptions will be allocated: □ Pro-rata basis □ First-come, first-served basis
□ Other – provide a description:_____
Maximum offering amount (if different from target offering amount): _____
Deadline to reach the target offering amount: _____

NOTE: If the sum of the investment commitments does not equal or exceed the target offering amount at the offering deadline, no securities will be sold in the offering, investment commitments will be cancelled and committed funds will be returned.

Current number of employees: _____

Total Assets:	Most recent fiscal year-end:	_____	Prior fiscal year-end:	_____
Cash & Cash Equivalents:	Most recent fiscal year-end:	_____	Prior fiscal year-end:	_____
Accounts Receivable:	Most recent fiscal year-end:	_____	Prior fiscal year-end:	_____
Short-term Debt:	Most recent fiscal year-end:	_____	Prior fiscal year-end:	_____
Long-term Debt:	Most recent fiscal year-end:	_____	Prior fiscal year-end:	_____
Revenues/Sales	Most recent fiscal year-end:	_____	Prior fiscal year-end:	_____
Cost of Goods Sold:	Most recent fiscal year-end:	_____	Prior fiscal year-end:	_____
Taxes Paid:	Most recent fiscal year-end:	_____	Prior fiscal year-end:	_____
Net Income:	Most recent fiscal year-end:	_____	Prior fiscal year-end:	_____

Using the list below, select the jurisdictions in which the issuer intends to offer the securities:

[List will include all U.S. jurisdictions, with an option to add and remove them individually, add all and remove all.]

GENERAL INSTRUCTIONS

I. Eligibility Requirements for Use of Form C

This Form shall be used for the offering statement, and any related amendments and progress reports, required to be filed by any issuer offering or selling securities in reliance on the exemption in Securities Act Section 4(a)(6) and in accordance with Section 4A and Regulation Crowdfunding (§ 227.100 *et seq.*). This Form also shall be used for an annual report required pursuant to Rule 202 of Regulation Crowdfunding (§ 227.202) and for the termination of reporting required pursuant to Rule 203(b)(2) of Regulation Crowdfunding (§ 227.203(b)(2)). Careful attention should be directed to the terms, conditions and requirements of the exemption.

II. Preparation and Filing of Form C

Information on the cover page will be generated based on the information provided in XML format. Other than the cover page, this Form is not to be used as a blank form to be filled in, but only as a guide in the preparation of Form C. General information regarding the preparation, format and how to file this Form is contained in Regulation S-T (§ 232 *et seq.*).

III. Information to be Included in the Form

Item 1. Offering Statement Disclosure Requirements

An issuer filing this Form for an offering in reliance on Section 4(a)(6) of the Securities Act and pursuant to Regulation Crowdfunding (§ 227.100 *et seq.*) must file the Form prior to the commencement of the offering and include the information required by Rule 201 of Regulation Crowdfunding (§ 227.201).

An issuer must include in the XML-based portion of this Form: the information required by paragraphs (a), (e), (g), (h), (l), (n), and (o) of Rule 201 of Regulation Crowdfunding (§ 227.201(a), (e), (g), (h), (l), (n), and (o)); selected financial data for the prior two fiscal years (including total assets, cash and cash equivalents, accounts

receivable, short-term debt, long-term debt, revenues/sales, cost of goods sold, taxes paid and net income); the jurisdictions in which the issuer intends to offer the securities; and any information required by Rule 203(a)(3) of Regulation Crowdfunding (§ 227.203(a)(3)).

Other than the information required to be provided in XML format, an issuer may provide the required information in the optional Question and Answer format included herein or in any other format included on the intermediary's platform, by filing such information as an exhibit to this Form, including copies of screen shots of the relevant information, as appropriate and necessary.

If disclosure in response to any paragraph of Rule 201 of Regulation Crowdfunding (§ 227.201) or Rule 203(a)(3) is responsive to one or more other paragraphs of Rule 201 of Regulation Crowdfunding (§ 227.201) or to Rule 203(a)(3) of Regulation Crowdfunding (§ 227.203(a)(3)), issuers are not required to make duplicate disclosures.

Item 2. Legends

(a) An issuer filing this Form for an offering in reliance on Section 4(a)(6) of the Securities Act and pursuant to Regulation Crowdfunding (§ 227.100 *et seq.*) must include the following legends:

> A crowdfunding investment involves risk. You should not invest any funds in this offering unless you can afford to lose your entire investment.
>
> In making an investment decision, investors must rely on their own examination of the issuer and the terms of the offering, including the merits and risks involved. These securities have not been recommended or approved by any federal or state securities commission or regulatory authority. Furthermore, these authorities have not passed upon the accuracy or adequacy of this document.
>
> The U.S. Securities and Exchange Commission does not pass upon the merits of any securities offered or the terms of the offering, nor does it pass upon the accuracy or completeness of any offering document or literature.
>
> These securities are offered under an exemption from registration; however, the U.S. Securities and Exchange Commission has not made an independent determination that these securities are exempt from registration.

(b) An issuer filing this Form for an offering in reliance on Section 4(a)(6) of the Securities Act and pursuant to Regulation Crowdfunding (§ 227.100 *et seq.*) must disclose in the offering statement that it will file a report with the Commission annually and post the report on its website, no later than 120 days after the end of each fiscal year covered by the report. The issuer must also disclose how an issuer may terminate its reporting obligations in the future in accordance with Rule 202(b) of Regulation Crowdfunding (§ 227.202(b)).

Item 3. Annual Report Disclosure Requirements

An issuer filing this Form for an annual report, as required by Regulation Crowdfunding (§ 227.100 *et seq.*), must file the Form no later than 120 days after the issuer's fiscal year end covered by the report and include the information required by Rule 201(a), (b), (c), (d), (e), (f), (m), (p), (q), (r), (s), (t), (x) and (y) of Regulation Crowdfunding (§§ 227.201(a), (b), (c), (d), (e), (f), (m), (p), (q), (r), (s), (t), (x) and (y)). For purposes of paragraph (t), the issuer shall provide financial statements certified by the principal executive officer of the issuer to be true and complete in all material respects. If, however, the issuer has available financial statements prepared in accordance with U.S. generally accepted accounting principles (U.S. GAAP) that have been reviewed or audited by an independent certified public accountant, those financial statements must be provided and the principal executive officer certification will not be required.

An issuer must include in the XML-based portion of this Form: the information required by paragraphs (a), and (e) of Rule 201 of Regulation Crowdfunding (§ 227.201(a) and (e)); and selected financial data for the prior two fiscal years (including total assets, cash and cash equivalents, accounts receivable, short-term debt, long-term debt, revenues/sales, cost of goods sold, taxes paid and net income).

SIGNATURE

Pursuant to the requirements of Sections 4(a)(6) and 4A of the Securities Act of 1933 and Regulation Crowdfunding (§ 227.100 *et seq.*), the issuer certifies that it has reasonable grounds to believe that it meets all of the requirements for filing on Form C and has duly caused this Form to be signed on its behalf by the duly authorized undersigned.

_____
(Issuer)

By

_____
(Signature and Title)

Pursuant to the requirements of Sections 4(a)(6) and 4A of the Securities Act of 1933 and Regulation Crowdfunding (§ 227.100 *et seq.*), this Form C has been signed by the following persons in the capacities and on the dates indicated.

_____
(Signature)

_____
(Title)

_____
(Date)

Instructions.

1. The form shall be signed by the issuer, its principal executive officer or officers, its principal financial officer, its controller or principal accounting officer and at least a majority of the board of directors or persons performing similar functions.

2. The name of each person signing the form shall be typed or printed beneath the signature.

Intentional misstatements or omissions of facts constitute federal criminal violations. *See* 18 U.S.C. 1001.

OPTIONAL QUESTION & ANSWER FORMAT

FOR AN OFFERING STATEMENT

Respond to each question in each paragraph of this part. Set forth each question and any notes, but not any instructions thereto, in their entirety. If disclosure in response to any question is responsive to one or more other questions, it is not necessary to repeat the disclosure. If a question or series of questions is inapplicable or the response is available elsewhere in the Form, either state that it is inapplicable, include a cross-reference to the responsive disclosure, or omit the question or series of questions.

Be very careful and precise in answering all questions. Give full and complete answers so that they are not misleading under the circumstances involved. Do not discuss any future performance or other anticipated event unless you have a reasonable basis to believe that it will actually occur within the foreseeable future. If any answer requiring significant information is materially inaccurate, incomplete or misleading, the Company, its management and principal shareholders may be liable to investors based on that information.

THE COMPANY

1. Name of issuer: _____

ELIGIBILITY

2. □ Check this box to certify that all of the following statements are true for the issuer:

- Organized under, and subject to, the laws of a State or territory of the United States or the District of Columbia.
- Not subject to the requirement to file reports pursuant to Section 13 or Section 15(d) of the Securities Exchange Act of 1934.
- Not an investment company registered or required to be registered under the Investment Company Act of 1940.
- Not ineligible to rely on this exemption under Section 4(a)(6) of the Securities Act as a result of a disqualification specified in Rule 503(a) of Regulation Crowdfunding. (For more information about these disqualifications, see Question 30 of this Question and Answer format).
- Has filed with the Commission and provided to investors, to the extent required, the ongoing annual reports required by Regulation Crowdfunding during the two years immediately preceding the filing of this offering statement (or for such shorter period that the issuer was required to file such reports).
- Not a development stage company that (a) has no specific business plan or (b) has indicated that its business plan is to engage in a merger or acquisition with an unidentified company or companies.

INSTRUCTION TO QUESTION 2: If any of these statements is not true, then you are NOT eligible to rely on this exemption under Section 4(a)(6) of the Securities Act.

3. Has the issuer or any of its predecessors previously failed to comply with the ongoing reporting requirements of Rule 202 of Regulation Crowdfunding? □ Yes □ No
Explain: _____

DIRECTORS OF THE COMPANY

4. Provide the following information about each director (and any persons occupying a similar status or performing a similar function) of the issuer:

Name: _____ Dates of Board Service: _____
Principal Occupation: _____
Employer: _____ Dates of Service: _____
Employer's principal business: _____

List all positions and offices with the issuer held and the period of time in which the director served in the position or office:

Position: _____ Dates of Service: _____
Position: _____ Dates of Service: _____
Position: _____ Dates of Service: _____

Business Experience: List the employers, titles and dates of positions held during past three years with an indication of job responsibilities:

Employer: _____
Employer's principal business: _____
Title: _____ Dates of Service: _____
Responsibilities: _____

Employer: _____
Employer's principal business: _____
Title: _____ Dates of Service: _____
Responsibilities: _____

Employer: _____
Employer's principal business: _____
Title: _____ Dates of Service: _____
Responsibilities: _____

OFFICERS OF THE COMPANY

5. Provide the following information about each officer (and any persons occupying a similar status or performing a similar function) of the issuer:

Name: _____
Title: _____ Dates of Service: _____
Responsibilities: _____

List any prior positions and offices with the issuer and the period of time in which the officer served in the position or office:

Position: _____ Dates of Service: _____
Responsibilities: _____

Position: _____ Dates of Service: _____
Responsibilities: _____

Position: _____ Dates of Service: _____
Responsibilities: _____

Business Experience: List any other employers, titles and dates of positions held during past three years with an indication of job responsibilities:

Employer: _____
Employer's principal business: _____
Title: _____ Dates of Service: _____
Responsibilities: _____

Employer: _____
Employer's principal business: _____
Title: _____ Dates of Service: _____
Responsibilities: _____

Employer: _____
Employer's principal business: _____
Title: _____ Dates of Service: _____
Responsibilities: _____

INSTRUCTION TO QUESTION 5: For purposes of this Question 5, the term officer means a president, vice president, secretary, treasurer or principal financial officer, comptroller or principal accounting officer, and any person routinely performing similar functions.

PRINCIPAL SECURITY HOLDERS

6. Provide the name and ownership level of each person, as of the most recent practicable date, who is the beneficial owner of 20 percent or more of the issuer's outstanding voting equity securities, calculated on the basis of voting power.

Name of Holder	No. and Class of Securities Now Held	% of Voting Power Prior to Offering
		%
		%
		%
		%

INSTRUCTION TO QUESTION 6: The above information must be provided as of a date that is no more than 120 days prior to the date of filing of this offering statement.

To calculate total voting power, include all securities for which the person directly or indirectly has or shares the voting power, which includes the power to vote or to direct the voting of such securities. If the person has the right to acquire voting power of such securities within 60 days, including through the exercise of any option, warrant or right, the conversion of a security, or other arrangement, or if securities are held by a member of the family, through corporations or partnerships, or otherwise in a manner that would allow a person to direct or control the voting of the securities (or share in such direction or control — as, for example, a co-trustee) they should be included as being "beneficially owned." You should include an explanation of these circumstances in a footnote to the "Number of and Class of Securities Now Held." To calculate outstanding voting equity securities, assume all outstanding options are exercised and all outstanding convertible securities converted.

BUSINESS AND ANTICIPATED BUSINESS PLAN

7. Describe in detail the business of the issuer and the anticipated business plan of the issuer.

RISK FACTORS

A crowdfunding investment involves risk. You should not invest any funds in this offering unless you can afford to lose your entire investment.

In making an investment decision, investors must rely on their own examination of the issuer and the terms of the offering, including the merits and risks involved. These securities have not been recommended or approved by any federal or state securities commission or regulatory authority. Furthermore, these authorities have not passed upon the accuracy or adequacy of this document.

The U.S. Securities and Exchange Commission does not pass upon the merits of any securities offered or the terms of the offering, nor does it pass upon the accuracy or completeness of any offering document or literature.

These securities are offered under an exemption from registration; however, the U.S. Securities and Exchange Commission has not made an independent determination that these securities are exempt from registration.

8. Discuss the material factors that make an investment in the issuer speculative or risky:

(1) _____

(2) _____

(3) _____

(4) _____

(5) _____

(6) _____

(7) _____

(8) _____

(9) _____

(10) _____

INSTRUCTION TO QUESTION 8: Avoid generalized statements and include only those factors that are unique to the issuer. Discussion should be tailored to the issuer's business and the offering and should not repeat the factors addressed in the legends set forth above. No specific number of risk factors is required to be identified. Add additional lines and number as appropriate.

THE OFFERING

9. What is the purpose of this offering?

10. How does the issuer intend to use the proceeds of this offering?

	If Target Offering Amount Sold	**If Maximum Amount Sold**
Total Proceeds	$	$
Less: Offering Expenses		
(A)		
(B)		
(C)		
Net Proceeds	$	$
Use of Net Proceeds		
(A)		
(B)		
(C)		
Total Use of Net Proceeds	$	$

INSTRUCTION TO QUESTION 10: An issuer must provide a reasonably detailed description of any intended use of proceeds, such that investors are provided with an adequate amount of information to understand how the offering proceeds will be used. If an issuer has identified a range of possible uses, the issuer should identify and describe each probable use and the factors the issuer may consider in allocating proceeds among the potential uses. If the issuer will accept proceeds in excess of the target offering amount, the issuer must describe the purpose, method for allocating oversubscriptions, and intended use of the excess proceeds with similar specificity.

11. How will the issuer complete the transaction and deliver securities to the investors?

12. How can an investor cancel an investment commitment?

NOTE: Investors may cancel an investment commitment until 48 hours prior to the deadline identified in these offering materials.

The intermediary will notify investors when the target offering amount has been met.

If the issuer reaches the target offering amount prior to the deadline identified in the offering materials, it may close the offering early if it provides notice about the new offering deadline at least five business days prior to such new offering deadline (absent a material change that would require an extension of the offering and reconfirmation of the investment commitment).

If an investor does not cancel an investment commitment before the 48-hour period prior to the offering deadline, the funds will be released to the issuer upon closing of the offering and the investor will receive securities in exchange for his or her investment.

If an investor does not reconfirm his or her investment commitment after a material change is made to the offering, the investor's investment commitment will be cancelled and the committed funds will be returned.

OWNERSHIP AND CAPITAL STRUCTURE

The Offering

13. Describe the terms of the securities being offered.

14. Do the securities offered have voting rights? □ Yes □ No

15. Are there any limitations on any voting or other rights identified above? □ Yes □ No
    Explain: _____

16. How may the terms of the securities being offered be modified?

Restrictions on Transfer of the Securities Being Offered

The securities being offered may not be transferred by any purchaser of such securities during the one-year period beginning when the securities were issued, unless such securities are transferred:

(1) to the issuer;
(2) to an accredited investor;
(3) as part of an offering registered with the U.S. Securities and Exchange Commission; or
(4) to a member of the family of the purchaser or the equivalent, to a trust controlled by the purchaser, to a trust created for the benefit of a member of the family of the purchaser or the equivalent, or in connection with the death or divorce of the purchaser or other similar circumstance.

NOTE: The term "accredited investor" means any person who comes within any of the categories set forth in Rule 501(a) of Regulation D, or who the seller reasonably believes comes within any of such categories, at the time of the sale of the securities to that person.

The term "member of the family of the purchaser or the equivalent" includes a child, stepchild, grandchild, parent, stepparent, grandparent, spouse or spousal equivalent, sibling, mother-in-law, father-in-law, son-in-law, daughter-in-law, brother-in-law, or sister-in-law of the purchaser, and includes adoptive relationships. The term "spousal equivalent" means a cohabitant occupying a relationship generally equivalent to that of a spouse.

Description of Issuer's Securities

17. What other securities or classes of securities of the issuer are outstanding? Describe the material terms of any other outstanding securities or classes of securities of the issuer.

Class of Security	Securities (or Amount) Authorized	Securities (or Amount) Outstanding	Voting Rights	Other Rights
Preferred Stock (list each class in order of preference):				
_____			□ Yes □ No	□ Yes □ No Specify: _____
_____			□ Yes □ No	□ Yes □ No Specify: _____
Common Stock:			□ Yes □ No	□ Yes □ No Specify: _____
Debt Securities:			□ Yes □ No	□ Yes □ No Specify: _____
Other:				
_____			□ Yes □ No	□ Yes □ No Specify: _____
_____			□ Yes □ No	□ Yes □ No Specify: _____

Class of Security	Securities Reserved for Issuance upon Exercise or Conversion
Warrants:	
Options:	
Other Rights:	
_____	
_____	

18. How may the rights of the securities being offered be materially limited, diluted or qualified by the rights of any other class of security identified above?

19. Are there any differences not reflected above between the securities being offered and each other class of security of the issuer? □ Yes □ No
Explain: _____

20. How could the exercise of rights held by the principal shareholders identified in Question 6 above affect the purchasers of the securities being offered?

21. How are the securities being offered being valued? Include examples of methods for how such securities may be valued by the issuer in the future, including during subsequent corporate actions.

22. What are the risks to purchasers of the securities relating to minority ownership in the issuer?

23. What are the risks to purchasers associated with corporate actions including:
    - additional issuances of securities,
    - issuer repurchases of securities,
    - a sale of the issuer or of assets of the issuer or
    - transactions with related parties?

24. Describe the material terms of any indebtedness of the issuer:

Creditor(s)	Amount Outstanding	Interest Rate	Maturity Date	Other Material Terms
	$_____	_____%		
	$_____	_____%		
	$_____	_____%		

25. What other exempt offerings has the issuer conducted within the past three years?

Date of Offering	Exemption Relied Upon	Securities Offered	Amount Sold	Use of Proceeds
			$_____	
			$_____	
			$_____	

26. Was or is the issuer or any entities controlled by or under common control with the issuer a party to any transaction since the beginning of the issuer's last fiscal year, or any currently proposed transaction, where the amount involved exceeds five percent of the aggregate amount of capital raised by the issuer in reliance on Section 4(a)(6) of the Securities Act during the preceding 12-month period, including the amount the issuer seeks to raise in the current offering, in which any of the following persons had or is to have a direct or indirect material interest:

    (1) any director or officer of the issuer;
    (2) any person who is, as of the most recent practicable date, the beneficial owner of 20 percent or more of the issuer's outstanding voting equity securities, calculated on the basis of voting power;
    (3) if the issuer was incorporated or organized within the past three years, any promoter of the issuer; or
    (4) any immediate family member of any of the foregoing persons.

    If yes, for each such transaction, disclose the following:

Specified Person	Relationship to Issuer	Nature of Interest in Transaction	Amount of Interest
			$_____

$_____
$_____

INSTRUCTIONS TO QUESTION 26:

The term transaction includes, but is not limited to, any financial transaction, arrangement or relationship (including any indebtedness or guarantee of indebtedness) or any series of similar transactions, arrangements or relationships.

Beneficial ownership for purposes of paragraph (2) shall be determined as of a date that is no more than 120 days prior to the date of filing of this offering statement and using the same calculation described in Question 6 of this Question and Answer format.

The term "member of the family" includes any child, stepchild, grandchild, parent, stepparent, grandparent, spouse or spousal equivalent, sibling, mother-in-law, father-in-law, son-in-law, daughter-in-law, brother-in-law, or sister-in-law of the person, and includes adoptive relationships. The term "spousal equivalent" means a cohabitant occupying a relationship generally equivalent to that of a spouse.

Compute the amount of a related party's interest in any transaction without regard to the amount of the profit or loss involved in the transaction. Where it is not practicable to state the approximate amount of the interest, disclose the approximate amount involved in the transaction.

FINANCIAL CONDITION OF THE ISSUER

27. Does the issuer have an operating history? □ Yes □ No

28. Describe the financial condition of the issuer, including, to the extent material, liquidity, capital resources and historical results of operations.

INSTRUCTIONS TO QUESTION 28:

The discussion must cover each year for which financial statements are provided. Include a discussion of any known material changes or trends in the financial condition and results of operations of the issuer during any time period subsequent to the period for which financial statements are provided.

For issuers with no prior operating history, the discussion should focus on financial milestones and operational, liquidity and other challenges.

For issuers with an operating history, the discussion should focus on whether historical results and cash flows are representative of what investors should expect in the future.

Take into account the proceeds of the offering and any other known or pending sources of capital. Discuss how the proceeds from the offering will affect liquidity, whether receiving these funds and any other additional funds is necessary to the viability of the business, and how quickly the issuer anticipates using its available cash. Describe the other available sources of capital to the business, such as lines of credit or required contributions by shareholders.

References to the issuer in this Question 28 and these instructions refer to the issuer and its predecessors, if any.

FINANCIAL INFORMATION

29. Include the financial information specified below covering the two most recently completed fiscal years or the period(s) since inception, if shorter:

Aggregate Offering Amount (defined below):	Financial Information Required:	Financial Statement Requirements:
(a) $100,000 or less:	• The following information or their equivalent line items as reported on the federal income tax return filed by the issuer for the most recently completed year (if any): o Total income o Taxable income; and o Total tax; certified by the principal executive officer of the issuer to reflect accurately the information reported on the issuer's federal income tax returns; and • Financial statements of the issuer and its predecessors, if any.	Financial statements must be **certified** by the principal executive officer of the issuer as set forth below. If financial statements are available that have either been reviewed or audited by a public accountant that is independent of the issuer, the issuer must provide those financial statements instead along with a signed audit or review report and need not include the information reported on the federal income tax returns or the certification of the principal executive officer.
(b) More than $100,000, but not more than $500,000:	• Financial statements of the issuer and its predecessors, if any.	Financial statements must be **reviewed** by a public accountant that is independent of the issuer and must include a signed review report. If financial statements of the issuer are available that have been audited by a public accountant that is independent of the issuer, the issuer must provide those financial statements instead along with a signed audit report and need not include the reviewed financial statements.
(c) More than $500,000:	• Financial statements of the issuer and its predecessors, if any.	If the issuer **has** previously sold securities in reliance on Regulation Crowdfunding: Financial statements must be **audited** by a public accountant that is independent of the issuer and must include a signed audit report. If the issuer **has not** previously sold securities in reliance on Regulation Crowdfunding and it is offering more than $500,000 but not more than

$1,000,000:	Financial statements must be **reviewed** by a public accountant that is independent of the issuer and must include a signed review report. If financial statements of the issuer are available that have been audited by a public accountant that is independent of the issuer, the issuer must provide those financial statements instead along with a signed audit report and need not include the reviewed financial statements.

INSTRUCTIONS TO QUESTION 29: To determine the financial statements required, the Aggregate Offering Amount for purposes of this Question 29 means the aggregate amounts offered and sold by the issuer, all entities controlled by or under common control with the issuer, and all predecessors of the issuer in reliance on Section 4(a)(6) of the Securities Act within the preceding 12-month period plus the current maximum offering amount provided on the cover of this Form.

To determine whether the issuer has previously sold securities in reliance on Regulation Crowdfunding for purposes of paragraph (c) of this Question 29, "issuer" means the issuer, all entities controlled by or under common control with the issuer, and all predecessors of the issuer.

Financial statements must be prepared in accordance with U.S. generally accepted accounting principles and must include balance sheets, statements of comprehensive income, statements of cash flows, statements of changes in stockholders' equity and notes to the financial statements. If the financial statements are not audited, they shall be labeled as "unaudited."

Issuers offering securities and required to provide the information set forth in row (a) before filing a tax return for the most recently completed fiscal year may provide information from the tax return filed for the prior year (if any), provided that the issuer provides information from the tax return for the most recently completed fiscal year when it is filed, if filed during the offering period. An issuer that requested an extension of the time to file would not be required to provide information from the tax return until the date when the return is filed, if filed during the offering period.

A principal executive officer certifying financial statements as described above must provide the following certification**:

> I, [identify the certifying individual], certify that:
>
> (1) the financial statements of [identify the issuer] included in this Form are true and complete in all material respects; and
>
> (2) the tax return information of [identify the issuer] included in this Form reflects accurately the information reported on the tax return for [identify the issuer] filed for the fiscal year ended [date of most recent tax return].
>
> [Signature]
> [Title]

** Intentional misstatements or omissions of facts constitute federal criminal violations. *See* 18 U.S.C. 1001.

To qualify as a public accountant that is independent of the issuer for purposes of this Question 29, the accountant must satisfy the independence standards of either:

(i) Rule 2-01 of Regulation S-X or

(ii) the AICPA.

The public accountant that audits or reviews the financial statements provided by an issuer must be (1) duly registered and in good standing as a certified public accountant under the laws of the place of his or her residence or principal office or (2) in good standing and entitled to practice as a public accountant under the laws of his or her place of residence or principal office.

An issuer will not be in compliance with the requirement to provide reviewed financial statement if the issuer received a review report that includes modifications. An issuer will not be in compliance with the requirement to provide audited financial statements if the issuer received a qualified opinion, an adverse opinion, or a disclaimer of opinion.

The issuer must notify the public accountant of the issuer's intended use of the public accountant's audit or review report in the offering.

For an offering conducted in the first 120 days of a fiscal year, the financial statements provided may be for the two fiscal years prior to the issuer's most recently completed fiscal year; however, financial statements for the two most recently completed fiscal years must be provided if they are otherwise available. If more than 120 days have passed since the end of the issuer's most recently completed fiscal year, the financial statements provided must be for the issuer's two most recently completed fiscal years. If the 120th day falls on a Saturday, Sunday, or holiday, the next business day shall be considered the 120th day for purposes of determining the age of the financial statements.

An issuer may elect to delay complying with any new or revised financial accounting standard until the date that a company that is not an issuer (as defined under section 2(a) of the Sarbanes-Oxley Act of 2002 is required to comply with such new or revised accounting standard, if such standard also applies to companies that are not issuers. Issuers electing such extension of time accommodation must disclose it at the time the issuer files its offering statement and apply the election to all standards. Issuers electing not to use this accommodation must forgo this accommodation for all financial accounting standards and may not elect to rely on this accommodation in any future filings

30. With respect to the issuer, any predecessor of the issuer, any affiliated issuer, any director, officer, general partner or managing member of the issuer, any beneficial owner of 20 percent or more of the issuer's outstanding voting equity securities, calculated in the same form as described in Question 6 of this Question and Answer format, any promoter connected with the issuer in any capacity at the time of such sale, any person that has been or will be paid (directly or indirectly) remuneration for solicitation of purchasers in connection with such sale of securities, or any general partner, director, officer or managing member of any such solicitor, prior to **[INSERT DATE 180 DAYS AFTER PUBLICATION IN THE FEDERAL REGISTER]**:

    (1) Has any such person been convicted, within 10 years (or five years, in the case of issuers, their predecessors and affiliated issuers) before the filing of this offering statement, of any felony or misdemeanor:

        (i) in connection with the purchase or sale of any security? □ Yes □ No

        (ii) involving the making of any false filing with the Commission? □ Yes □ No

(iii) arising out of the conduct of the business of an underwriter, broker, dealer, municipal securities dealer, investment adviser, funding portal or paid solicitor of purchasers of securities? □ Yes □ No

If Yes to any of the above, explain: _____

(2) Is any such person subject to any order, judgment or decree of any court of competent jurisdiction, entered within five years before the filing of the information required by Section 4A(b) of the Securities Act that, at the time of filing of this offering statement, restrains or enjoins such person from engaging or continuing to engage in any conduct or practice:

(i) in connection with the purchase or sale of any security? □ Yes □ No;

(ii) involving the making of any false filing with the Commission? □ Yes □ No

(iii) arising out of the conduct of the business of an underwriter, broker, dealer, municipal securities dealer, investment adviser, funding portal or paid solicitor of purchasers of securities? □ Yes □ No

If Yes to any of the above, explain: _____

(3) Is any such person subject to a final order of a state securities commission (or an agency or officer of a state performing like functions); a state authority that supervises or examines banks, savings associations or credit unions; a state insurance commission (or an agency or officer of a state performing like functions); an appropriate federal banking agency; the U.S. Commodity Futures Trading Commission; or the National Credit Union Administration that:

(i) at the time of the filing of this offering statement bars the person from:

(A) association with an entity regulated by such commission, authority, agency or officer? □ Yes □ No

(B) engaging in the business of securities, insurance or banking? □ Yes □ No

(C) engaging in savings association or credit union activities? □ Yes □ No

(ii) constitutes a final order based on a violation of any law or regulation that prohibits fraudulent, manipulative or deceptive conduct and for which the order was entered within the 10-year period ending on the date of the filing of this offering statement? □ Yes □ No

If Yes to any of the above, explain: _____

(4) Is any such person subject to an order of the Commission entered pursuant to Section 15(b) or 15B(c) of the Exchange Act or Section 203(e) or (f) of the Investment Advisers Act of 1940 that, at the time of the filing of this offering statement:

(i) suspends or revokes such person's registration as a broker, dealer, municipal securities dealer, investment adviser or funding portal? □ Yes □ No

(ii) places limitations on the activities, functions or operations of such person? □ Yes □ No

(iii) bars such person from being associated with any entity or from participating in the offering of any penny stock? □ Yes □ No

If Yes to any of the above, explain: _____

(5) Is any such person subject to any order of the Commission entered within five years before the filing of this offering statement that, at the time of the filing of this offering statement, orders the person to cease and desist from committing or causing a violation or future violation of:

(i) any scienter-based anti-fraud provision of the federal securities laws, including without limitation Section 17(a)(1) of the Securities Act, Section 10(b) of the

Exchange Act, Section 15(c)(1) of the Exchange Act and Section 206(1) of the Investment Advisers Act of 1940 or any other rule or regulation thereunder?
□ Yes □ No

(ii) Section 5 of the Securities Act? □ Yes □ No

If Yes to either of the above, explain: _____

(6) Is any such person suspended or expelled from membership in, or suspended or barred from association with a member of, a registered national securities exchange or a registered national or affiliated securities association for any act or omission to act constituting conduct inconsistent with just and equitable principles of trade?
□ Yes □ No
If Yes, explain: _____

(7) Has any such person filed (as a registrant or issuer), or was any such person or was any such person named as an underwriter in, any registration statement or Regulation A offering statement filed with the Commission that, within five years before the filing of this offering statement, was the subject of a refusal order, stop order, or order suspending the Regulation A exemption, or is any such person, at the time of such filing, the subject of an investigation or proceeding to determine whether a stop order or suspension order should be issued?
□ Yes □ No
If Yes, explain: _____

(8) Is any such person subject to a United States Postal Service false representation order entered within five years before the filing of the information required by Section 4A(b) of the Securities Act, or is any such person, at the time of filing of this offering statement, subject to a temporary restraining order or preliminary injunction with respect to conduct alleged by the United States Postal Service to constitute a scheme or device for obtaining money or property through the mail by means of false representations?
□ Yes □ No
If Yes, explain: _____

If you would have answered "Yes" to any of these questions had the conviction, order, judgment, decree, suspension, expulsion or bar occurred or been issued after [INSERT DATE 180 DAYS AFTER PUBLICATION IN THE FEDERAL REGISTER], then you are NOT eligible to rely on this exemption under Section 4(a)(6) of the Securities Act.

INSTRUCTIONS TO QUESTION 30: Final order means a written directive or declaratory statement issued by a federal or state agency, described in Rule 503(a)(3) of Regulation Crowdfunding, under applicable statutory authority that provides for notice and an opportunity for hearing, which constitutes a final disposition or action by that federal or state agency.

No matters are required to be disclosed with respect to events relating to any affiliated issuer that occurred before the affiliation arose if the affiliated entity is not (i) in control of the issuer or (ii) under common control with the issuer by a third party that was in control of the affiliated entity at the time of such events.

OTHER MATERIAL INFORMATION

31. In addition to the information expressly required to be included in this Form, include:
    (1) any other material information presented to investors; and
    (2) such further material information, if any, as may be necessary to make the required statements, in the light of the circumstances under which they are made, not misleading.

INSTRUCTIONS TO QUESTION 31: If information is presented to investors in a format, media or other means not able to be reflected in text or portable document format, the issuer should include

(a) a description of the material content of such information;
(b) a description of the format in which such disclosure is presented; and
(c) in the case of disclosure in video, audio or other dynamic media or format, a transcript or description of such disclosure.

ONGOING REPORTING

The issuer will file a report electronically with the Securities & Exchange Commission annually and post the report on its website, no later than:

_____

(120 days after the end of each fiscal year covered by the report).

Once posted, the annual report may be found on the issuer's website at:

_____

The issuer must continue to comply with the ongoing reporting requirements until:

(1) the issuer is required to file reports under Section 13(a) or Section 15(d) of the Exchange Act;
(2) the issuer has filed at least one annual report pursuant to Regulation Crowdfunding and has fewer than 300 holders of record and has total assets that do not exceed $10,000,000;
(3) the issuer has filed at least three annual reports pursuant to Regulation Crowdfunding;
(4) the issuer or another party repurchases all of the securities issued in reliance on Section 4(a)(6) of the Securities Act, including any payment in full of debt securities or any complete redemption of redeemable securities; or
(5) the issuer liquidates or dissolves its business in accordance with state law.

* * * * *

PART 240 - GENERAL RULES AND REGULATIONS, SECURITIES EXCHANGE ACT OF 1934

8. The authority citation for part 240 continues to read, in part, as follows:

Authority: 15 U.S.C. 77c, 77d, 77g, 77j, 77s, 77z-2, 77z-3, 77eee, 77ggg, 77nnn, 77sss, 77ttt, 78c, 78c-3, 78c-5, 78d, 78e, 78f, 78g, 78i, 78j, 78j-1, 78k, 78k-1, 78l, 78m, 78n, 78n-1, 78o, 78o-4, 78o-10, 78p, 78q, 78q-1, 78s, 78u-5, 78w, 78x, 78ll, 78mm, 80a-20, 80a-23, 80a-29, 80a-37, 80b-3, 80b-4, 80b-11, 7201 et. seq., and 8302; 7 U.S.C. 2(c)(2)(E); 12 U.S.C. 5221(e)(3); 18 U.S.C. 1350; and Pub. L. 111-203, 939A, 124 Stat. 1376, (2010), unless otherwise noted.

9. Add § 240.12g-6 to read as follows:

§ 240.12g-6 Exemption for securities issued pursuant to Section 4(a)(6) of the Securities Act of 1933.

For purposes of determining whether an issuer is required to register a security with the Commission pursuant to Section 12(g)(1) of the Act (15 U.S.C. 78l(g)(1)), the definition of held of record shall not include securities issued pursuant to the offering exemption under Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6)) by an issuer that:

(a) is current in filing its ongoing annual reports required pursuant to § 227.202 of this chapter;

(b) has total assets not in excess of $25 million as of the end of its most recently completed fiscal year; and

(c) has engaged a transfer agent registered pursuant to Section 17A(c) of the Act to perform the function of a transfer agent with respect to such securities.

An issuer that would be required to register a class of securities under Section 12(g) of the Act as a result of exceeding the asset threshold in subparagraph (b) may continue to exclude the relevant securities from the definition of "held of record" for a transition period ending on the penultimate day of the fiscal year two years after the date it became ineligible. The transition period terminates immediately upon the failure of an issuer to timely file any periodic report due pursuant to § 227.202 at which time the issuer must file a registration statement that registers that class of securities under the Act within 120 days.

* * * * *

PART 249 – FORMS, SECURITIES EXCHANGE ACT OF 1934

10. The authority citation for part 249 continues to read, in part, as follows:

Authority: 15 U.S.C. 78a et seq. and 7201 et seq.; 12 U.S.C. 5461 et seq.; and 18 U.S.C. 1350, unless otherwise noted.

* * * * *

11. Add subpart U, consisting of § 249.2000 to read as follows:

Subpart U – Forms for Registration of Funding Portals

§ 249.2000 Form Funding Portal

This form shall be used for filings by funding portals under Regulation Crowdfunding (§§ 227.100 *et seq.*).

Note: The text of Form Funding Portal will not appear in the Code of Federal Regulations.

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM FUNDING PORTAL

APPLICATION OR AMENDMENT TO APPLICATION FOR REGISTRATION OR WITHDRAWAL FROM REGISTRATION AS FUNDING PORTAL UNDER THE SECURITIES EXCHANGE ACT OF 1934

WARNING: Failure to complete this form truthfully, to keep this form current and to file accurate supplementary information on a timely basis, or the failure to keep accurate books and records or otherwise to comply with the provisions of law applying to the conduct of business as a *funding portal*, would violate the Federal securities laws and may result in disciplinary, administrative, injunctive or criminal action.

Check the appropriate box:
This is:
□ an initial application to register as a *funding portal* with the *SEC*.
□ an amendment to any part of the *funding portal*'s most recent Form Funding Portal, including a *successor* registration.
□ a withdrawal of the *funding portal*'s registration with the *SEC*.

Schedule A must be completed as part of all initial applications. Amendments to Schedule A must be provided on Schedule B. Schedule C must be completed by *nonresident funding portals.* If this is a withdrawal of a *funding portal*'s registration, complete Schedule D.

If this is an amendment to any part of the *funding portal's* most recent Form Funding Portal, provide an explanation describing the amendment: _____

_____

Item 1 – Identifying Information

Exact name, principal business address, mailing address, if different, and contact information of the *funding portal*:

A. Full name of the *funding portal*: _____

B. Name(s)/Website URL(s) under which business is conducted, if different from Item 1A:
_____

C. IRS Empl. Ident. No.: _____

D. If a name and/or website URL in (1A) or (1B) has changed since the *funding portal*'s most recent Form Funding Portal, enter the previous name and/or website URL and specify whether the name change is of the □ *funding portal* name (1A), or □ name/website URL (1B).

Previous name(s) or website URL(s): _____

E. *Funding portal*'s main street address (Do not use a P.O. Box):

_____

_____

F. Mailing address(es) (if different) and office locations (if more than one):

_____

_____

G. Contact Information:
Telephone Number: _____
Fax Number: _____
Email Address: _____

H. Contact Employee Information:
Name: _____
Title: _____
Direct Telephone Number: _____
Fax Number: _____
Direct Email Address: _____

I. Month *applicant*'s fiscal year ends: _____

J. Registrations

Was the *applicant* previously registered on Form Funding Portal as a *funding portal* or with the Commission in any other capacity?

□ Yes SEC File No.: _____
□ No

K. Foreign registrations

(1) Is the *applicant* registered with a *foreign financial regulatory authority*? Answer "no" even if affiliated with a business that is registered with a *foreign financial regulatory authority*.

□ Yes □ No

If "yes," complete Section K.2. below.

(2) List the name, in English, of each *foreign financial regulatory authority* and country with which the *applicant* is registered. A separate entry must be completed for each *foreign financial regulatory authority* with which the *applicant* is registered.

English Name of *Foreign Financial Regulatory Authority*:

_____

Registration Number (if any): _____

Name of Country: _____

Item 2 – Form of Organization

A. Indicate legal status of *applicant*.

☐ Corporation ☐ Limited Liability Company
☐ Sole Proprietorship ☐ Other (please specify) _____
☐ Partnership

B. If other than a sole proprietor, indicate date and place *applicant* obtained its legal status (*i.e.*, state or country where incorporated, where partnership agreement was filed, or where *applicant* entity was formed):

State/Country of formation: _____
Date of formation: _____

Item 3 – Successions

A. Is the *applicant* at the time of this filing succeeding to the business of a currently registered *funding portal*?

□ Yes □ No

Do not report previous successions already reported on Form Funding Portal. If "yes," complete Section 3.B. below.

B. Complete the following information if succeeding to the business of a currently-registered *funding portal*. If the *applicant* acquired more than one *funding portal* in the succession being reported on this Form Funding Portal, a separate entry must be completed for each acquired firm.

Name of Acquired *Funding Portal*:

_____

Acquired *Funding Portal*'s *SEC* File No.: _____

C. Briefly describe details of the succession including any assets or liabilities not assumed by the *successor*.

Item 4 – Control Relationships

In this Item, identify every *person* that, directly or indirectly, *controls* the *applicant*, *controls* management or policies of the *applicant*, or that the *applicant* directly or indirectly *controls*.

_____

_____

If this is an initial application, the *applicant* also must complete Schedule A. Schedule A asks for information about direct owners and executive officers. If this is an amendment updating information reported on the Schedule A filed with the *applicant*'s initial application, the *applicant* must complete Schedule B.

Item 5 – Disclosure Information

In this Item, provide information about the *applicant*'s disciplinary history and the disciplinary history of all *associated persons* or *control affiliates* of the *applicant* (as applicable). This information is used to decide whether to revoke registration, to place limitations on the *applicant*'s activities as a *funding portal*, and to identify potential problem areas on which to focus during examinations. One event may result in the requirement to answer "yes" to more than one of the questions below. Check all answers that apply. Refer to the Explanation of Terms section of Form Funding Portal Instructions for explanation of italicized terms.

If the answer is "yes" to any question in this Item, the *applicant* must complete the appropriate Disclosure Reporting Page ("DRP") (FP) – Criminal, Regulatory Action, Civil Judicial Action, Bankruptcy/SIPC, Bond, or Judgment/Lien, as applicable.

Criminal Disclosure

If the answer is "yes" to any question below, complete a Criminal DRP.

A. In the past ten years, has the *applicant* or any *associated person*:

(1) been convicted of any *felony*, or pled guilty or nolo contendere ("no contest") to any charge of a *felony*, in a domestic, foreign, or military court?

□ Yes □ No

The response to the following question may be limited to charges that are currently pending:

(2) been *charged* with any *felony*?

□ Yes □ No

B. In the past ten years, has the *applicant* or any *associated person*:

(1) been convicted of any *misdemeanor*, or pled guilty or nolo contendere ("no contest"), in a domestic, foreign, or military court to any charge of a *misdemeanor* in a case involving: *investment-related* business, or any fraud, false statements, or omissions, wrongful taking of property, bribery, perjury, forgery, counterfeiting, extortion, or a conspiracy to commit any of these offenses?

□ Yes □ No

The response to the following question may be limited to charges that are currently pending:

(2) been *charged* with a *misdemeanor* listed in Item 5-B(1)?

□ Yes □ No

Regulatory Action Disclosure

If the answer is "yes" to any question below, complete a Regulatory Action DRP.

C. Has the *SEC* or the Commodities Futures Trading Commission ("CFTC") ever:

(1) *found* the *applicant* or any *associated person* to have made a false statement or omission?

□ Yes □ No

(2) *found* the *applicant* or any *associated person* to have been *involved* in a violation of any *SEC* or CFTC regulations or statutes?

□ Yes □ No

(3) *found* the *applicant* or any *associated person* to have been a cause of the denial, suspension, revocation, or restriction of the authorization of an *investment-related* business to operate?

□ Yes □ No

(4) entered an *order* against the *applicant* or any *associated person* in connection with *investment-related* activity?

□ Yes □ No

(5) imposed a civil money penalty on the *applicant* or any *associated person*, or ordered the *applicant* or any *associated person* to cease and desist from any activity?

□ Yes □ No

D. Has any other federal regulatory agency, any state regulatory agency, or any *foreign financial regulatory authority*:

(1) ever *found* the *applicant* or any *associated person* to have made a false statement or omission, or been dishonest, unfair, or unethical?

□ Yes □ No

(2) ever *found* the *applicant* or any *associated person* to have been *involved* in a violation of *investment-related* regulations or statutes?

□ Yes □ No

(3) ever *found* the *applicant* or any *associated person* to have been the cause of a denial, suspension, revocation, or restriction of the authorization of an *investment-related* business to operate?

□ Yes □ No

(4) in the past ten years entered an *order* against the *applicant* or any *associated person* in connection with an *investment-related* activity?

□ Yes □ No

(5) ever denied, suspended, or revoked the registration or license of the *applicant* or that of any *associated person*, or otherwise prevented the *applicant* or any *associated person* of the *applicant*, by *order*, from associating with an *investment-related* business or restricted the activities of the *applicant* or any *associated person*?

□ Yes □ No

E. Has any *self-regulatory organization* or commodities exchange ever:

(1) *found* the *applicant* or any *associated person* to have made a false statement or omission?

□ Yes □ No

(2) *found* the *applicant* or any *associated person* to have been *involved* in a violation of its rules (other than a violation designated as a *minor rule violation* under a plan approved by the *SEC*)?

□ Yes □ No

(3) *found* the *applicant* or any *associated person* to have been the cause of a denial, suspension, revocation or restriction of the authorization of an *investment-related* business to operate?

□ Yes □ No

(4) disciplined the *applicant* or any *associated person* by expelling or suspending the *applicant* or the *associated person* from membership, barring or suspending the *applicant* or *the associated person* from association with other members, or by otherwise restricting the activities of the *applicant* or the *associated person*?

□ Yes □ No

F. Has the *applicant* or any *associated person* ever had an authorization to act as an attorney, accountant, or federal contractor revoked or suspended?

□ Yes □ No

G. Is the *applicant* or any *associated person* currently the subject of any regulatory *proceeding* that could result in a "yes" answer to any part of Item 5-C, 5-D, or 5-E?

□ Yes □ No

Civil Judicial Disclosure

If the answer is "yes" to a question below, complete a Civil Judicial Action DRP.

H. Has any domestic or foreign court:

(1) in the past ten years, *enjoined* the *applicant* or any *associated person* in connection with any *investment-related* activity?

□ Yes □ No

(2) ever *found* that the *applicant* or any *associated person* was *involved* in a violation of *investment-related* statutes or regulations?

□ Yes □ No

(3) ever dismissed, pursuant to a settlement agreement, an *investment- related* civil action brought against the *applicant* or any *associated person* by a state or *foreign financial regulatory authority*?

□ Yes □ No

I. Is the *applicant* or any *associated person* now the subject of any civil *proceeding* that could result in a "yes" answer to any part of Item 5-H(1)-(3)?

□ Yes □ No

Financial Disclosure

If the answer is "yes" to a question below, complete a Bankruptcy/Disclosure, Bond Disclosure or Judgment/Lien DRP, as applicable.

J. In the past ten years, has the *applicant* or a *control affiliate* of the *applicant* ever been a securities firm or a *control affiliate* of a securities firm that:

(1) has been the subject of a bankruptcy petition?

□ Yes □ No

(2) has had a trustee appointed or a direct payment procedure initiated under the Securities Investor Protection Act?

□ Yes □ No

K. Has a bonding company ever denied, paid out on, or revoked a bond for the *applicant*?

□ Yes □ No

L. Does the *applicant* have any unsatisfied judgments or liens against it?

□ Yes □ No

Item 6 – Non-Securities Related Business

Does *applicant* engage in any non-securities related business?

□ Yes □ No

If "yes," briefly describe the non-securities business.

_____

_____

Item 7 – Qualified Third Party Arrangements; Compensation Arrangements

A. Qualified Third Party Arrangements. Complete the following information for each *person* that will hold investor funds in escrow or otherwise pursuant to the requirements of Rule 303(e) of Regulation Crowdfunding (17 CFR 227.303(e)).

Name of *person*: _____

Address: _____

Phone Number: _____

B. Compensation. Please describe any compensation arrangements *funding portal* has with issuers.

_____

EXECUTION

The *funding portal* consents that service of any civil action brought by or notice of any proceeding before the Securities and Exchange Commission or any *self-regulatory organization* in connection with the *funding portal*'s investment-related business may be given by registered or certified mail to the *funding portal*'s contact *person* at the main address, or mailing address, if different, given in Items 1.E., 1.F., and 1.H. If the applicant is a *nonresident funding portal*, it must complete Schedule C to designate a U.S. agent for service of process.

The undersigned represents and warrants that he/she has executed this form on behalf of, and is duly authorized to bind, the *funding portal*. The undersigned and the *funding portal* represent that the information and statements contained herein and other information filed herewith, all of which are made a part hereof, are current, true and complete. The undersigned and the *funding portal* further represent that, if this is an amendment, to the extent that any information previously submitted is not amended, such information is currently accurate and complete.

Date: _____

Full Legal Name of *Funding Portal*: _____

By:_____
(signature)

Title: _____

FORM FUNDING PORTAL
SCHEDULE A

Direct Owners and Executive Officers

1. Complete Schedule A only if submitting an initial application. Schedule A asks for information about the *applicant*'s direct owners and executive officers. Use Schedule B to amend this information.

2. Direct Owners and Executive Officers. List below the names of:

   (a) each Chief Executive Officer, Chief Financial Officer, Chief Operations Officer, Chief Legal Officer, Chief Compliance Officer, director and any other individuals with similar status or functions;

   (b) if *applicant* is organized as a corporation, each shareholder that is a direct owner of 5% or more of a class of the *applicant*'s voting securities, unless *applicant* is a public reporting company (a company subject to Section 13 or 15(d) of the Exchange Act);

   Direct owners include any *person* that owns, beneficially owns, has the right to vote, or has the power to sell or direct the sale of 5% or more of a class of the *applicant*'s voting securities. For purposes of this Schedule, a *person* beneficially owns any securities: (i) owned by his/her child, stepchild, grandchild, parent, stepparent, grandparent, spouse, sibling, mother-in-law, father-in-law, son-in-law, daughter-in-law, brother-in-law, or sister-in-law, sharing the same residence; or (ii) that he/she has the right to acquire, within 60 days, through the exercise of any option, warrant, or right to purchase the security.

   (c) if the *applicant* is organized as a partnership, <u>all</u> general partners and those limited and special partners that have the right to receive upon dissolution, or have contributed, 5% or more of the *applicant*'s capital;

   (d) in the case of a trust, (i) a *person* that directly owns 5% or more of a class of the *applicant*'s voting securities, or that has the right to receive upon dissolution, or has contributed, 5% or more of the *applicant*'s capital, (ii) the trust and (iii) each trustee; and

   (e) if the *applicant* is organized as a limited liability company ("LLC"), (i) those members that have the right to receive upon dissolution, or have contributed, 5% or more of the *applicant*'s capital, and (ii) if managed by elected managers, all elected managers.

3. In the DE/FE/NP column below, enter "DE" if the owner is a domestic entity, "FE" if the owner is an entity incorporated or domiciled in a foreign country, or "NP" if the owner or executive officer is a natural person.

4. Complete the Title or Status column by entering board/management titles; status as partner, trustee, sole proprietor, elected manager, shareholder, or member; and for shareholders or members, the class of securities owned (if more than one is issued).

5. Ownership codes are:

NA - less than 5%	B - 10% but less than 25%	D - 50% but less than 75%
A - 5% but less than 10%	C - 25% but less than 50%	E - 75% or more
	G - Other (general partner, trustee, or elected member)	

6. Control Person:
   (a) In the Control Person column, enter "Yes" if the *person* has *control* as defined in the Glossary of Terms to Form Funding Portal, and enter "No" if the *person* does not have *control*. Note that under this definition, most executive officers and all 25% owners, general partners, elected managers, and trustees are "control persons".

   (b) In the PR column, enter "PR" if the owner is a public reporting company under Section 13 or 15(d) of the Exchange Act.

7. Complete each column.

FULL LEGAL NAME (Natural Persons: Last Name, First Name, Middle Name)	**DE/FE/NP**	**Title or Status**	**Date Title or Status Acquired**		**Ownership Code**	**Control Person**		***CRD* No. (If None: S.S. No. and Date of Birth, IRS Tax No., or IRS Employer ID No.)**
			MM	YYYY		Yes/No	PR	

FORM FUNDING PORTAL
SCHEDULE B

Amendments to Schedule A

1. Use Schedule B only to amend information requested on Schedule A. Refer to Schedule A for specific instructions for completing this Schedule B. Complete each column. File with a completed Execution Page.

2. In the Type of Amendment column, indicate "A" (addition), "D" (deletion), or "C" (change in information about the same *person*).

3. Ownership codes are:

NA - less than 5%	B - 10% but less than 25%	D - 50% but less than 75%
A - 5% but less than 10%	C - 25% but less than 50%	E - 75% or more
	G - Other (general partner, trustee, or elected member)	

4. List below all changes to Schedule A (Direct Owners and Executive Officers):

FULL LEGAL NAME (Natural Persons: Last Name, First Name, Middle	**DE/FE/NP**	**Type of Amendment**	**Title or Status**	**Date Title or Status Acquired**		**Ownership Code**	**Control Person**		***CRD* No. (If None: S.S. No. and Date of Birth, IRS Tax No., or IRS Employer ID No.)**
				MM	YYYY		Yes/No	PR	

FORM FUNDING PORTAL
SCHEDULE C

Nonresident Funding Portals

Service of Process and Certification Regarding Prompt Access to Books and Records and Ability to Submit to Inspections and Examinations

Each *nonresident funding portal applicant* shall use Schedule C of Form Funding Portal to: identify its United States agent for service of process, and certify that it can, as a matter of law and will: (1) provide the Commission and any registered national securities association of which it becomes a member with prompt access to its books and records, and (2) submit to onsite inspection and examination by the Commission and any registered national securities association of which it becomes a member.

A. Agent for Service of Process:

1. Name of United States *person applicant* designates and appoints as agent for service of process:

   _____

2. Address of United States *person applicant* designates and appoints as agent for service of process

   _____

The above identified agent for service of process may be served any process, pleadings, subpoenas, or other papers in:

(a) any investigation or administrative proceeding conducted by the Commission that relates to the *applicant* or about which the *applicant* may have information; and

(b) any civil or criminal suit or action or proceeding under the federal securities laws brought against the *applicant* or to which the *applicant* has been joined as defendant or respondent, in any appropriate court in any place subject to the jurisdiction of any state or of the United States or of any of its territories or possessions or of the District of Columbia. The *applicant* has stipulated and agreed that any such suit, action or administrative proceeding may be commenced by the service of process upon, and that service of an administrative subpoena shall be effected by service upon, the above-named agent for service of process, and that service as aforesaid shall be taken and held in all courts and administrative tribunals to be valid and binding as if personal service thereof had been made.

B. Certification regarding access to records and ability to submit to inspections and examinations:

Applicant can, as a matter of law, and will:

1. provide the Commission and any registered national securities association of which it becomes a member with prompt access to its books and records, and

2. submit to onsite inspection and examination by the Commission and any registered national securities association of which it becomes a member.

Applicant must attach as an exhibit to this Form Funding Portal, Exhibit C, a copy of the opinion of counsel it is required to obtain in accordance with Rule 400(f) of Regulation Crowdfunding, i.e., the opinion of counsel that the nonresident funding portal can, as a matter of law, provide the Commission and any registered national securities association of which the nonresident funding portal becomes a member with prompt access to the books and records of such nonresident funding portal, and that the nonresident funding portal can, as a matter of law, submit to onsite inspection and examination by the Commission and any registered national securities association of which the nonresident funding portal becomes a member.

EXECUTION FOR NON-RESIDENT FUNDING PORTALS

The undersigned represents and warrants that he/she has executed this form on behalf of, and is duly authorized to bind, the *nonresident funding portal*. The undersigned and the *nonresident funding portal* represent that the information and statements contained herein and other information filed herewith, all of which are made a part hereof, are current, true and complete. The undersigned and the *nonresident funding portal* further represent that, if this is an amendment, to the extent that any information previously submitted is not amended, such information is currently accurate and complete.

The undersigned certifies that the *nonresident funding portal* can, as a matter of law, and will provide the Commission and any registered national securities association of which it becomes a member with prompt access to the books and records of such *nonresident funding portal* and can, as a matter of law, and will submit to onsite inspection and examination by the Commission and any registered national securities association of which it becomes a member. Finally, the undersigned authorizes any person having custody or possession of these books and records to make them available to federal regulatory representatives.

Signature: _____

Name and Title: _____

Date: _____

FORM FUNDING PORTAL
SCHEDULE D

If this is a withdrawal of registration:

A. The date the *funding portal* ceased business or withdrew its registration request:
Date (MM/DD/YYYY): _____

B. Location of Books and Records after Registration Withdrawal

Complete the following information for each location at which the *applicant* will keeps books and records after withdrawing its registration.

Name and address of entity where books and records are kept:

_____

_____

_____
(area code)(telephone number) (area code) (fax number)

This is (check one): ☐ one of *applicant*'s branch offices or affiliates.
☐ a third party unaffiliated recordkeeper.
☐ other.

If this address is a private residence, check this box: ☐

Briefly describe the books and records kept at this location.

_____
_____
_____
_____

C. Is the *funding portal* now the subject of or named in any *investment-related*

1. Investigation

□ Yes □ No

2. Investor initiated complaint

□ Yes □ No

3. Private civil litigation

□ Yes □ No

CRIMINAL ACTION DISCLOSURE REPORTING PAGE (FP)

General Instructions

This Disclosure Reporting Page (DRP FP) is an ☐ INITIAL ***OR*** ☐ AMENDED response used to report details for affirmative responses to Items 5-A or 5-B of Form Funding Portal.

Check item(s) being responded to: ☐ 5-A(1) ☐ 5-A(2) ☐ 5-B(1) ☐ 5-B(2)

Use a separate DRP for each event or *proceeding*. The same event or *proceeding* may be reported for more than one *person* or entity using one DRP. File with a completed Execution Page.

Multiple counts of the same charge arising out of the same event(s) should be reported on the same DRP. Unrelated criminal actions, including separate cases arising out of the same event, must be reported on separate DRPs. Use this DRP to report all charges arising out of the same event. One event may result in more than one affirmative answer to the items listed above.

Part 1

Check all that apply:

1. The *person*(s) or entity(ies) for whom this DRP is being filed is (are) the:

   Select only one.

   ☐ *Applicant*
   ☐ *Applicant* and one or more *associated persons*
   ☐ One or more of *applicant*'s *associated persons*

If this DRP is being filed for the *applicant*, and it is an amendment that seeks to remove a DRP concerning the *applicant* from the record, the reason the DRP should be removed is:

☐ The *applicant* is registered or applying for registration, and the event or *proceeding* was resolved in the *applicant*'s favor.
☐ The DRP was filed in error.

If this DRP is being filed for an *associated person*:

This *associated person* is: ☐ a firm ☐ a natural person
The *associated person* is: ☐ registered with the *SEC* ☐ not registered with the *SEC*

Full name of the *associated person* (including, for natural persons, last, first and middle names):

_____

If the *associated person* has a *CRD* number, provide that number. _____

If this is an amendment that seeks to remove a DRP concerning the *associated person*, the reason the DRP should be removed is:

- ☐ The *associated person* (s) is (are) no longer associated with the *applicant*.
- ☐ The event or *proceeding* was resolved in the *associated person*'s favor.
- ☐ The event or *proceeding* occurred more than ten years ago.
- ☐ The DRP was filed in error. Explain the circumstances:

_____

_____

Part 2

1. If charge(s) were brought against a firm or organization over which the *applicant* or a *associated person* exercise(s)(d) *control*:

   A. Enter the firm or organization's name _____

   B. Was the firm or organization engaged in an *investment-related* business?

   ☐ Yes ☐ No

   C. What was the relationship of the *applicant* with the firm or organization? (In the case of a *associated person*, include any position or title with the firm or organization.)

   _____

2. Court where formal charge(s) were brought in: (include the name of Federal, Military, State or Foreign Court, Location of Court - City or County and State or Country, and Docket/Case number).

   A. Name of Court: _____

   B. Location of Court:

   Street Address: _____
   City or County: _____ State/Country: _____
   Postal Code: _____

   C. Docket/Case Number: _____

3. Event Disclosure Detail (Use this for both organizational and individual charges.)

   A. Date First *Charged* (MM/DD/YYYY): _____ ☐ Exact

   ☐ Explanation

If not exact, provide explanation:

_____

B. Event Disclosure Detail (include charge(s)/charge Description(s), and for each charg*e* provide: (1) number of counts, (2) *felony* or *misdemeanor*, (3) plea for each charge, and (4) product type if charge is *investment-related*).

_____

C. Did any of the charge(s) within the event *involve* a *felony*? ☐ Yes ☐ No

D. Current status of the event? ☐ Pending ☐ On Appeal ☐ Final

E. Event status date (Complete unless status is pending)

(MM/DD/YYYY): _____ ☐ Exact
☐ Explanation

If not exact, provide explanation:

_____

4. Disposition Disclosure Detail: Include for each charge (a) Disposition Type (e.g., convicted, acquitted, dismissed, pretrial, etc.), (b) Date, (c) Sentence/Penalty, (d) Duration (if sentence-suspension, probation, etc.), (e) Start Date of Penalty, (f) Penalty/Fine Amount, and (g) Date Paid.

_____

5. Provide a brief summary of circumstances leading to the charge(s) as well as the disposition. Include the relevant dates when the conduct that was the subject of the charge(s) occurred. (The response must fit within the space provided.)

_____

_____

REGULATORY ACTION DISCLOSURE REPORTING PAGE (FP)

GENERAL INSTRUCTIONS

This Disclosure Reporting Page (DRP FP) is an ☐ INITIAL ***OR*** ☐ AMENDED response used to report details for affirmative responses to Item 5-C, 5-D, 5-E-5-F or 5-G of Form Funding Portal.

Check item(s) being responded to: ☐ 5-C(1) ☐ 5-C(2) ☐ 5-C(3) ☐ 5-C(4)
☐ 5-C(5) ☐ 5-D(1) ☐ 5-D(2) ☐ 5-D(3) ☐ 5-D(4) ☐ 5-D(5)
☐ 5-E(1) ☐ 5-E(2) ☐ 5-E(3) ☐ 5-E(4) ☐ 5-F ☐ 5-G

Use a separate DRP for each event or *proceeding*. An event or *proceeding* may be reported for more than one *person* or entity using one DRP. File with a completed Execution Page.

One event may result in more than one affirmative answer to Items 5-C, 5-D, 5-E, 5- F or 5-G. Use only one DRP to report details related to the same event. If an event gives rise to actions by more than one regulator, provide details for each action on a separate DRP.

Part 1

The *person*(s) or entity(ies) for whom this DRP is being filed is (are) the:

Select only one.

☐ *Applicant* (the *funding portal*)
☐ *Applicant* and one or more of the *applicant*'s *associated person* (s)
☐ One or more of *applicant*'s *associated person* (s)

If this DRP is being filed for the *applicant* and it is an amendment that seeks to remove a DRP concerning the *applicant* from the record, the reason the DRP should be removed is:

☐ The *applicant* is registered or applying for registration, and the event or *proceeding* was resolved in the *applicant*'s favor.
☐ The DRP was filed in error.

If this DRP is being filed for an *associated person*:

This *associated person* is: ☐ a firm
☐ a natural person

The *associated person is*: ☐ registered with the *SEC*
☐ not registered with the *SEC*

Full name of the *associated person* (including, for natural persons, last, first and middle names):

_____

If the *associated person* has a *CRD* number, provide that number. _____

If this is an amendment that seeks to remove a DRP concerning the *associated person*, the reason the DRP should be removed is:

- ☐ The *associated person* (s) is (are) no longer associated with the *applicant*.
- ☐ The event or *proceeding* was resolved in the *associated person*'s favor.
- ☐ The DRP was filed in error. Explain the circumstances:

_____

_____

Part 2

1. Regulatory Action was initiated by:

☐ *SEC* ☐ Other Federal Authority ☐ *SRO*
☐ Foreign Authority ☐ State

(Full name of regulator, *foreign financial regulatory authority*, federal authority, state or *SRO*)

_____

_____

_____

2. Principal Sanction (check appropriate item):

☐ Civil and Administrative Penalty(ies)/Fine(s)

☐ Restitution	☐ Expulsion	☐ Disgorgement
☐ Bar	☐ Revocation	☐ Suspension
☐ Cease and Desist	☐ Injunction	☐ Undertaking
☐ Censure	☐ Prohibition	☐ Other
☐ Denial	☐ Reprimand	

Other Sanctions:

_____

_____

_____

3. Date Initiated (MM/DD/YYYY): _____ ☐ Exact
☐ Explanation

If not exact, provide explanation:

_____
_____
_____
_____

4. Docket/Case Number: _____

5. *Associated person*'s Employing Firm when activity occurred that led to the regulatory action (if applicable):

_____
_____
_____

6. Principal Product Type (check appropriate item):

☐ Annuity(ies) - Fixed	☐ Derivative(s)	☐ Mutual Fund(s)
☐ Annuity(ies) - Variable	☐ Direct Investment(s) - DPP & LP Interest(s)	
☐ Money Market Fund(s)	☐ Equity - OTC	☐ Options
☐ CD(s)	☐ Equity Listed (Common & Preferred Stock)	
☐ Commodity Option(s)	☐ Futures - Commodity	☐ Penny Stock(s)
☐ Debt - Asset Backed	☐ Futures - Financial	☐ Unit Investment Trust(s)
☐ Debt - Corporate	☐ Index Option(s)	☐ Other
☐ Debt - Government	☐ Insurance	☐ No Product
☐ Debt - Municipal	☐ Investment Contract(s)	

Other Product Types:

_____
_____
_____

7. Describe the allegations related to this regulatory action. (The response must fit within the space provided.)

_____
_____
_____

8. Current status? ☐ Pending ☐ On Appeal ☐ Final

9. If on appeal, to whom the regulatory action was appealed (*SEC*, *SRO*, Federal or State Court) and date appeal filed:

_____

_____

If Final or On Appeal, complete all items below. For Pending Actions, complete Item 13 only.

10. How was matter resolved (check appropriate item):

☐ Acceptance, Waiver & Consent (AWC)
☐ Consent
☐ Decision
☐ Decision & *Order* of Offer of Settlement
☐ Dismissed
☐ Withdrawn
☐ Settled
☐ Stipulation and Consent
☐ Vacated
☐ *Order*
☐ Other

11. Resolution Date (MM/DD/YYYY): _____ ☐ Exact ☐ Explanation

If not exact, provide explanation:

_____

_____

12. Resolution Detail:

A. Were any of the following Sanctions Ordered (check all appropriate items)?

☐ Monetary/Fine
Amount: $_____
☐ Bar
☐ Revocation/Expulsion/Denial
☐ Disgorgement
☐ Cease & Desist/Injunction
☐ Censure
☐ Suspension

B. Other Sanctions Ordered:

_____

_____

C. Sanction detail: If suspended, *enjoined* or barred, provide duration including start date and capacities affected (General Securities Principal, Financial Operations Principal, etc.). If requalification by exam/retraining was a condition of the sanction, provide length of time given to requalify/retrain, type of exam required and whether condition has been satisfied. If disposition resulted in a fine, penalty, restitution, disgorgement or monetary compensation, provide total amount, portion levied against the *applicant* or an *associated person*, date paid and if any portion of penalty was waived:

_____

_____

13. Provide a brief summary of details related to the action status and (or) disposition, and include relevant terms, conditions and dates.

_____

CIVIL JUDICIAL ACTION DISCLOSURE REPORTING PAGE (FP)

GENERAL INSTRUCTIONS

This Disclosure Reporting Page (DRP FP) is an ☐ INITIAL ***OR*** ☐ AMENDED response used to report details for affirmative responses to Item 5-H or 5-I of Form Funding Portal.

Check item(s) being responded to: ☐ 5-H(1) ☐ 5-H(2) ☐ 5-H(3) ☐ 5-I

Use a separate DRP for each event or *proceeding*. An event or *proceeding* may be reported for more than one *person* or entity using one DRP. File with a completed Execution Page.

One event may result in more than one affirmative answer to Item 5-H or 5-I. Use only one DRP to report details related to the same event. Unrelated civil judicial actions must be reported on separate DRPs.

Part 1

The *person*(s) or entity(ies) for whom this DRP is being filed is (are) the:

Select only one.

☐ *Applicant* (the *funding portal*)
☐ *Applicant* and one or more of the applicant's *associated person* (s)
☐ One or more of the *applicant*'s associated *person* (s)

If this DRP is being filed for the *applicant* and it is an amendment that seeks to remove a DRP concerning the *applicant* from the record, the reason the DRP should be removed is:

☐ The *applicant* is registered or applying for registration, and the event or *proceeding* was resolved in the *applicant*'s favor.
☐ The DRP was filed in error.

If this DRP is being filed for an *associated person*:

This *associated person* is: ☐ a firm ☐ a natural person
The *associated person*: ☐ registered with the *SEC* ☐ not registered with the *SEC*

Full name of the *associated person* (including, for natural persons, last, first and middle names):

_____

If the *associated person* has a *CRD* number, provide that number. _____

If this is an amendment that seeks to remove a DRP concerning the *associated person*, the reason the DRP should be removed is:

☐ The *associated person* (s) is (are) no longer associated with the *applicant*.
☐ The event or *proceeding* was resolved in the *associated person*'s favor.
☐ The DRP was filed in error. Explain the circumstances:

_____

_____

Part 2

1. Court Action initiated by: (Name of regulator, *foreign financial regulatory authority*, *SRO*, commodities exchange, agency, firm, private plaintiff, etc.)

2. Principal Relief Sought (check appropriate item):

☐ Cease and Desist (Private/Civil Complaint)	☐ Disgorgement	☐ Money Damages
☐ Restraining Order	☐ Civil Penalty(ies)/Fine(s)	
☐ Injunction	☐ Restitution	
☐ Other _____		

Other Relief Sought: _____

3. Filing Date of Court Action (MM/DD/YYYY): _____ ☐ Exact ☐ Explanation

   If not exact, provide explanation:

   _____

4. Principal Product Type (check appropriate item):

☐ Annuity(ies) - Fixed	☐ Derivative(s)	☐ Investment Contract(s)
☐ Annuity(ies) - Variable	☐ Direct Investment(s) – DPP & LP Interest(s)	
☐ Money Market Fund(s)	☐ CD(s)	☐ Equity - OTC
☐ Mutual Fund(s)	☐ Commodity Option(s)	☐ No Product
☐ Equity Listed (Common & Preferred Stock)		☐ Options
☐ Debt - Asset Backed	☐ Futures - Commodity	☐ Penny Stock(s)
☐ Debt - Corporate	☐ Futures - Financial	☐ Unit Investment Trust(s)
☐ Debt - Government	☐ Index Option(s)	☐ Other
☐ Debt - Municipal	☐ Insurance	

Other Product Types:

_____

5. Formal Action was brought in (include the name of the Federal, State, or Foreign Court; Location of Court – City or County and State or Country; and Docket/Case Number

_____

6. *Associated person*'s Employing Firm when activity occurred that led to the civil judicial action (if applicable):

_____

7. Describe the allegations related to this civil action (the response must fit within the space provided):

_____

_____

8. Current status? ☐ Pending ☐ On Appeal ☐ Final

9. If on appeal, court to which the action was appealed (provide name of the court) and Date Appeal Filed (MM/DD/YYYY):

_____

_____

10. If pending, date notice/process was served (MM/DD/YYYY): _____

☐ Exact ☐ Explanation

If not exact, provide explanation:

_____

If Final or On Appeal, complete all items below. For Pending Actions, complete Item 14 only.

11. How was matter resolved (check appropriate item):

☐ Consent ☐ Judgment Rendered ☐ Settled ☐ Dismissed ☐ Opinion
☐ Withdrawn ☐ Other _____

12. Resolution Date (MM/DD/YYYY): _____ ☐ Exact
☐ Explanation

If not exact, provide explanation:

_____

_____

13. Resolution Detail:

A. Were any of the following Sanctions Ordered or Relief Granted (check appropriate items)?

☐ Monetary/Fine
Amount: $ _____
☐ Bar
☐ Revocation/Expulsion/Denial
☐ Censure
☐ Suspension
☐ Disgorgement/Restitution
☐ Cease and Desist/Injunction

B. Other Sanctions Ordered:

_____
_____
_____

C. Sanction detail: If suspended, *enjoined* or barred, provide duration including start date and capacities affected (General Securities Principal, Financial Operations Principal, etc.). If requalification by exam/retraining was a condition of the sanction, provide length of time given to requalify/retrain, type of exam required and whether condition has been satisfied. If disposition resulted in a fine, penalty, restitution, disgorgement or monetary compensation, provide total amount, portion levied against the *applicant* or an *associated person*, date paid and if any portion of penalty was waived:

_____
_____
_____
_____
_____
_____

14. Provide a brief summary of circumstances related to the action(s), allegation(s), disposition(s) and/or finding(s) disclosed above.

_____
_____
_____

BANKRUPTCY/SIPC DISCLOSURE REPORTING PAGE (FP)

GENERAL INSTRUCTIONS

This Disclosure Reporting Page (DRP FP) is an ☐ INITIAL ***OR*** ☐ AMENDED response used to report details for affirmative responses to Item 5-J of Form Funding Portal.

Check item(s) being responded to: ☐ 5-J(1) ☐ 5-J(2)

Use a separate DRP for each event or *proceeding*. An event or *proceeding* may be reported for more than one *person* or entity using one DRP. File with a completed Execution Page.

One event may result in more than one affirmative answer to Item 5-J. Use only one DRP to report details related to the same event. Unrelated civil judicial actions must be reported on separate DRPs.

Part 1

1. The *person*(s) or entity(ies) for whom this DRP is being filed is (are) the:

   Select only one.

   ☐ *Applicant*
   ☐ *Applicant* and one or more *control affiliate*(s)
   ☐ One or more of *control affiliate*(s)

If this DRP is being filed for a *control affiliate*, give the full name of the *control affiliate* below (for individuals, Last name, First name, Middle name).

If the *control affiliate* is registered with the CRD, provide the CRD number. If not, indicate "non-registered'' by checking the appropriate checkbox.

FP DRP - CONTROL AFFILIATE

_____
Control Affiliate CRD Number

This *control affiliate* is: ☐ a firm
☐ a natural person

Registered: ☐ Yes ☐ No

Full name of the *control affiliate* (including, for natural persons, last, first and middle names):

_____

☐ This is an amendment that seeks to remove a DRP record because the *control affiliate*(s) is (are) no longer associated with the *funding portal*.

2. If the *control affiliate* is registered through the CRD, has the *control affiliate* submitted a DRP (with Form U-4) or BD DRP to the CRD System for the event? If the answer is "Yes,'' no other information on this DRP must be provided.

Yes ☐ No ☐

NOTE: The completion of this Form does not relieve the *control affiliate* of its obligation to update its CRD records.

Part 2

1. Action Type: (check appropriate item)

☐ Bankruptcy ☐ Declaration ☐ Receivership

☐ Compromise ☐ Liquidated ☐ Other_____

2. Action Date (MM/DD/YYYY):_____ ☐ Exact

☐ Explanation

If not exact, provide explanation:_____

3. If the financial action relates to an organization over which the *applicant* or *control affiliate person* exercise(s)(d) *control*, enter organization name and the *applicant*'s or *control affiliate*'s position, title or relationship:

_____

Was the Organization *investment-related*? ☐ Yes ☐ No

4. Court action brought in (Name of Federal, State or Foreign Court), Location of Court (City or County and State or Country), Docket/Case Number and Bankruptcy Chapter Number (if Federal Bankruptcy Filing):

_____

5. Is action currently pending? ☐ Yes ☐ No

6. If not pending, provide Disposition Type: (check appropriate item)

☐ Direct Payment Procedure ☐ Dismissed ☐ Satisfied/Released
☐ Discharged ☐ Dissolved ☐ SIPA Trustee Appointed

☐ Other _____

7. Disposition Date (MM/DD/YYYY): ☐ Exact ☐ Explanation

If not exact, provide explanation: _____

8. Provide a brief summary of events leading to the action, and if not discharged, explain. (The information must fit within the space provided):

_____

9. If a SIPA trustee was appointed or a direct payment procedure was begun, enter the amount paid by you; or the name of trustee:

Currently Open? ☐ Yes ☐ No

Date Direct Payment Initiated/Filed or Trustee Appointed (MM/DD/YYYY):_____

☐ Exact ☐ Explanation

If not exact, provide explanation:_____

10. Provide details to any status disposition. Include details as to creditors, terms, conditions, amounts due and settlement schedule (if applicable):_____

BOND DISCLOSURE REPORTING PAGE (FP)

GENERAL INSTRUCTIONS

This Disclosure Reporting Page (DRP FP) is an ☐ INITIAL ***OR*** ☐ AMENDED response used to report details for affirmative responses to Item 5-K of Form Funding Portal.

Check item(s) being responded to: ☐ 5-K

Use a separate DRP for each event or *proceeding*. An event or *proceeding* may be reported for more than one *person* or entity using one DRP. File with a completed Execution Page.

One event may result in more than one affirmative answer to Item 5-K. Use only one DRP to report details related to the same event. If an event gives rise to actions by more than one regulator, provide details for each action on a separate DRP.

1. Firm Name: (Policy Holder)

_____

2. Bonding Company Name:

_____

3. Disposition Type: (check appropriate item)

   ☐ Denied ☐ Payout ☐ Revoked

4. Disposition Date (MM/DD/YYYY): ☐ Exact ☐ Explanation

   If not exact, provide explanation:

_____
_____
_____

5. If disposition resulted in Payout, list Payout Amount and Date Paid:

_____
_____
_____

6. Summarize the details of circumstances leading to the necessity of the bonding company action:

_____
_____
_____
_____
_____

JUDGMENT / LIEN DISCLOSURE REPORTING PAGE (FP)

GENERAL INSTRUCTIONS

This Disclosure Reporting Page (DRP FP) is an ☐ INITIAL ***OR*** ☐ AMENDED response used to report details for affirmative responses to Item 5-L of Form Funding Portal.

Check item(s) being responded to: ☐ 5-L

Use a separate DRP for each event or *proceeding*. An event or *proceeding* may be reported for more than one *person* or entity using one DRP. File with a completed Execution Page. One event may result in more than one affirmative answer to Item 5-L. Use only one DRP to report details related to the same event. If an event gives rise to actions by more than one regulator, provide details for each action on a separate DRP.

1. Judgment/Lien Amount:_____
2. Judgment/Lien Holder:_____

3. Judgment/Lien Type: (check appropriate item)

   ☐ Civil ☐ Default ☐ Tax

4. Date Filed (MM/DD/YYYY):_____ ☐ Exact
   ☐ Explanation

   If not exact, provide explanation: _____

5. Is Judgment/Lien outstanding? ☐ Yes ☐ No

   If No, provide explanation:_____

   If No, how was matter resolved? (check appropriate item)

   ☐ Discharged ☐ Released ☐ Removed ☐ Satisfied

6. Court where judgment was given:

   A. Name of Court _____

   B. Location of Court:
      Street Address: _____
      City or County: _____ State/Country: _____
      Postal Code: _____

   C. Docket/Case Number _____

7. Provide a brief summary of events leading to the action and any payment schedule details, including current status (if applicable):_____

FORM FUNDING PORTAL INSTRUCTIONS

A. GENERAL INSTRUCTIONS

1. EXPLANATION OF FORM

- This is the form that a *funding portal* must use to register with the Securities and Exchange Commission ("SEC" or "Commission"), to amend its registration and to withdraw from registration.
- The Commission may make publicly accessible all current Forms Funding Portal, including amendments and registration withdrawal requests, which may be searchable by the public, with the exception of certain personally identifiable information or other information with significant potential for misuse (including the contact employee's direct phone number, fax number and e-mail address and any IRS Tax Number, IRS Employer Identification Number, social security number, date of birth, or any other similar information). If the *applicant* submits any attachments to Form Funding Portal in PDF format it is the responsibility of the *applicant* to redact certain personally identifiable information or other information with significant potential for misuse (including the contact employee's direct phone number, fax number and e-mail address and any IRS Tax Number, IRS Employer Identification Number, social security number, date of birth, or any other similar information) from the PDF.

2. WHEN TO FILE FORM FUNDING PORTAL

- A *funding portal*'s registration must become effective before offering or selling any securities in reliance on Section 4(a)(6) through a platform. Under Rule 400, a *funding portal*'s registration will be effective the later of: (1) 30 calendar days after the date a complete Form Funding Portal is received by the Commission or (2) the date the *funding portal* is approved for membership by a national securities association registered under Section 15A of the Securities Exchange Act of 1934 ("Exchange Act").

- A registered *funding portal* must promptly file an amendment to Form Funding Portal when any information previously submitted on Form Funding Portal becomes inaccurate or incomplete for any reason.

- A *successor funding portal* may succeed to the registration of a registered *funding portal* by filing a registration on Form Funding Portal within 30 days after the succession.

- If a *funding portal* succeeds to and continues the business of a registered *funding portal* and the succession is based solely on a change of the predecessor's date or state of incorporation, form of organization, or composition of a partnership or similar reason, the *successor* may, within 30 days of the succession, amend the registration on Form Funding Portal to reflect these changes.

- A *funding portal* must also file a withdrawal on Form Funding Portal (and complete Schedule D) promptly upon ceasing to operate as a *funding portal*. Withdrawal will be effective on the later of 30 days after receipt by the Commission, after the *funding portal* is no longer operational, or within such longer period of time as to which the *funding portal* consents or which the Commission by order may determine as necessary or appropriate in the public interest or for the protection of investors.

- A Form Funding Portal filing will not be considered complete unless it complies with all applicable requirements.

3. ELECTRONIC FILING – The *applicant* must file Form Funding Portal electronically, and must utilize this system to file and amend Form Funding Portal electronically to assure the timely acceptance and processing of those filings.

4. CONTACT EMPLOYEE – The individual listed as the contact employee must be authorized to receive all compliance information, communications, and mailings, and be responsible for disseminating it within the *applicant*'s organization.

5. FEDERAL INFORMATION LAW AND REQUIREMENTS

- The principal purpose of this form is to provide a mechanism by which a *funding portal* can register with the Commission, amend its registration and withdraw from registration. The Commission maintains a file of the information on this form and will make certain information collected through the form publicly available. The SEC will not accept forms that do not include the required information.

- Section 4A(a) of the Securities Act of 1933 [15 U.S.C. §77d-1(a)] and Sections 3(h) and 23(a) the Exchange Act [15 U.S.C. §§78c(h) and 78w(a)] authorize the SEC to collect the information required by Form Funding Portal. The SEC collects the information for regulatory purposes. Filing Form Funding Portal is mandatory for *persons* that are registering as *funding portals* with the SEC.

- Any member of the public may direct to the Commission any comments concerning the accuracy of the burden estimate on this Form and any suggestions for reducing this burden. This collection of information has been reviewed by the Office of Management and Budget in accordance with the clearance requirements of 44 U.S.C. §3507. The information contained in this form is part of a system of records subject to the Privacy Act of 1974, as amended. The Securities and Exchange Commission has published in the Federal Register the Privacy Act Systems of Records Notice for these records.

B. FILING INSTRUCTIONS

1. FORMAT

- All fields requiring a response in Items 1-7 must be completed before the filing will be accepted.

- *Applicant* must complete the execution page certifying that Form Funding Portal and amendments thereto have been executed properly and that the information contained therein is accurate and complete.

- To amend information, the *applicant* must update the appropriate Form Funding Portal pages or Schedules.

- A paper copy, with original manual signatures, of the initial Form Funding Portal filing and amendments to Form Funding Portal and Disclosure Reporting Pages must be retained by the *applicant* and be made available for inspection upon a regulatory request.

2. **DISCLOSURE REPORTING PAGES (DRP)** – Information concerning the *applicant* or *associated person* that relates to the occurrence of an event reportable under Item 5 must be provided on the *applicant*'s appropriate DRP (FP). If an *associated person* is an individual or organization registered through the CRD, such *associated person* need only complete the *associated person* name and CRD number of the *applicant*'s appropriate DRP. Details for the event must be submitted on the *associated person*'s appropriate DRP or DRP (U-4). If an *associated person* is an individual or organization not registered through the CRD, provide complete answers to all of the questions and complete all fields requiring a response on the *associated person*'s appropriate DRP (FP).

3. **DIRECT OWNERS** - Amend the Direct Owners and Executive Officers page when changes in ownership occur.

4. **NONRESIDENT APPLICANTS –** Any *applicant* that is a *nonresident funding portal* must complete Schedule C and attach the opinion of counsel referred to therein.

C. EXPLANATION OF TERMS

1. GENERAL

APPLICANT - The *funding portal* applying on or amending this form.

ASSOCIATED PERSON - Any partner, officer, director or manager of the funding portal (or any person occupying a similar status or performing similar functions), any person directly or indirectly controlling or controlled by the funding portal, or any employee of the funding portal, except that any person associated with a funding portal whose functions are solely clerical or ministerial shall not be included in the meaning of such term for purposes of section 15(b) of the Exchange Act (other than paragraphs (4) and (6) thereof).

CONTROL - The power, directly or indirectly, to direct the management or policies of the *funding portal*, whether through contract, or otherwise. A *person* is presumed to *control* a *funding portal* if that *person*: (1) is a director, general partner or officer exercising executive responsibility (or has a similar status or functions); (2) directly or indirectly has the right to vote 25 percent or more of a class of a voting security or has the power to sell or direct the sale of 25 percent or more of a class of voting securities of the *funding portal*; or (3) in the case of a partnership, has contributed, or has a right to receive, 25 percent or more of the capital of the *funding portal*. (This definition is used solely for the purposes of Form Funding Portal).

CONTROL AFFILIATE – A *person* named in Item 4 or any other individual or organization that directly or indirectly controls, is under common control with, or is controlled by, the *applicant*, including any current employee of the *applicant* except one performing only clerical, administrative, support or similar functions, or who, regardless of title, performs no executive duties or has no senior policy making authority.

FOREIGN FINANCIAL REGULATORY AUTHORITY – Includes (1) a foreign securities authority; (2) other governmental body or foreign equivalent of a *self-regulatory organization* empowered by a foreign government to administer or enforce its laws relating to the regulation of *investment* or *investment-related* activities*;* and (3) a foreign membership organization, a function of which is to regulate the participation of its members in the activities listed above.

FUNDING PORTAL - A broker acting as an intermediary in a transaction involving the offer or sale of securities offered and sold in reliance on Section 4(a)(6), that does not, directly or indirectly: (1) offer *investment* advice or recommendations; (2) solicit purchases, sales or offers to buy the securities displayed on its platform; (3) compensate employees, agents, or other *persons* for such solicitation or based on the sale of securities displayed or referenced on its platform; or (4) hold, manage, possess, or otherwise handle investor funds or securities.

JURISDICTION – Any state of the United States, the District of Columbia, the Commonwealth of Puerto Rico, the U.S. Virgin Islands, any other territory of the United States, or any subdivision or regulatory body thereof.

NONRESIDENT FUNDING PORTAL – A *funding portal* incorporated in or organized under the laws of a jurisdiction outside of the United States or its territories, or having its principal place of business in any place not in the United States or its territories.

PERSON - An individual, partnership, corporation, trust, or other organization.

SELF-REGULATORY ORGANIZATION ("SRO") – A national securities association registered under Section 15A of the Exchange Act or any national securities exchange or registered clearing agency.

SUCCESSOR –A *funding portal* that assumes or acquires substantially all of the assets and liabilities, and that continues the business of, a registered predecessor *funding portal* that ceases its *funding portal* activities. *See* Rule 400(c) of Regulation Crowdfunding (17 CFR 227.400(c)).

2. FOR THE PURPOSE OF ITEM 5 AND THE CORRESPONDING DISCLOSURE REPORTING PAGES (DRPs) (FP)

CHARGED - Being accused of a crime in a formal complaint, information, or indictment (or equivalent formal charge).

ENJOINED – Includes being subject to a mandatory injunction, prohibitory injunction, preliminary injunction, or temporary restraining order.

FELONY – For *jurisdictions* that do not differentiate between a *felony* and a *misdemeanor*, a *felony* is an offense punishable by a sentence of at least one year imprisonment and/or a fine of at least $1,000. The term also includes a general court martial.

FOUND – Includes adverse final actions, including consent decrees in which the respondent has neither admitted nor denied the findings, but does not include agreements, deficiency letters, examination reports, memoranda of understanding, letters of caution, admonishments, and similar informal resolutions of matters.

INVESTMENT OR INVESTMENT-RELATED – Pertaining to securities, commodities, banking, savings association activities, credit union activities, insurance, or real estate (including, but not limited to, acting as or being associated with a *funding portal* broker-dealer, municipal securities dealer, government securities broker or dealer, issuer, investment company, investment adviser, futures sponsor, bank, security-based swap dealer, major security-based swap participant, savings association, credit union, insurance company, or insurance agency).

INVOLVED – Doing an act or aiding, abetting, counseling, commanding, inducing, conspiring with or failing reasonably to supervise another in doing an act.

MINOR RULE VIOLATION – A violation of a *self-regulatory organization* rule that has been designated as "minor" pursuant to a plan approved by the SEC or Commodity Futures Trading Commission. A rule violation may be designated as "minor" under a plan if the sanction imposed consists of a fine of $2,500 or less and if the sanctioned *person* does not contest the fine. (Check with the appropriate *self-regulatory organization* to determine if a particular rule violation has been designated as "minor" for these purposes).

MISDEMEANOR – For *jurisdictions* that do not differentiate between a *felony* and a *misdemeanor*, a *misdemeanor* is an offense punishable by a sentence of less than one year

imprisonment and/or a fine of less than $1,000. The term also includes a special court martial.

ORDER – A written directive issued pursuant to statutory authority and procedures, including orders of denial, suspension, or revocation; does not include special stipulations, undertakings or agreements relating to payments, limitations on activity or other restrictions unless they are included in an *order*.

PROCEEDING – Includes a formal administrative or civil action initiated by a governmental agency, *self-regulatory organization* or a *foreign financial regulatory authority*; a *felony* criminal indictment or information (or equivalent formal charge); or a *misdemeanor* criminal information (or equivalent formal charge). Does not include other civil litigation, investigations, or arrests or similar charges effected in the absence of a formal criminal indictment or information (or equivalent formal charge).

* * * * *

PART 269 – FORMS PRESCRIBED UNDER THE TRUST INDENTURE ACT OF 1939

12. The authority citation for part 269 continues to read as follows:

Authority: 15 U.S.C. 77ddd(c), 77eee, 77ggg, 77hhh, 77iii, 77jjj, 77sss, and 78ll(d), unless otherwise noted.

* * * * *

PART 274 – FORMS PRESCRIBED UNDER THE INVESTMENT COMPANY ACT OF 1940

13. The authority citation for part 274 continues to read, in part, as follows:

Authority: 15 U.S.C. 77f, 77g, 77h, 77j, 77s, 78c(b), 78l, 78m, 78n, 78o(d), 80a–8, 80a–24, 80a–26, and 80a–29, unless otherwise noted.

* * * * *

14. Form ID (referenced in §§239.63, 249.446, 269.7 and 274.402 of this chapter) is amended by adding a check box that reads “Funding Portal” in alphabetical order in the list of applicants in Part I; and the Instructions to Form ID are amended to include the definition of “Funding Portal” in alphabetical order under Part I and reads “Funding Portal: A broker acting as

an intermediary in a transaction involving the offer or sale of securities offered and sold in reliance on Section 4(a)(6) of the Securities Act, that does not: (1) offer investment advice or recommendations; (2) solicit purchases, sales or offers to buy the securities displayed on its platform; (3) compensate employees, agents, or other persons for such solicitation or based on the sale of securities displayed or referenced on its platform; or (4) hold, manage, possess, or otherwise handle investor funds or securities."

(Note: The amendments to Form ID will not appear in the Code of Federal Regulations.)

By the Commission.

Jill M. Peterson
Assistant Secretary

Date: October 30, 2015

EXHIBIT A

Comment Letters Received Regarding Proposing Release
to Implement Regulation Crowdfunding (File No. S7-09-13)

AABOC:	Letter from Doby Gavn, President and CEO, African American Business Opportunities Communities, Oct. 26, 2013
ABA:	Letter from Catherine T. Dixon, Chair, Federal Regulation of Securities Committee, Business Law Section, American Bar Association
Accredify:	Letter from Herwig G. Konings, CEO, Accredify LLC, Nov. 30, 2013
Active Agenda:	Letter from Daniel F. Zahlis, Founder, Product Architect, Active Agenda LLC, Jan. 29, 2014
Advanced Hydro:	Letter from Dileep Agnihotri, Ph.D., CEO, Advanced Hydro Inc., Oct. 23, 2013
AEO:	Letter from Connie E. Evans, President & CEO, Association for Enterprise Opportunity, Feb. 3, 2014
AFL-CIO:	Letter from Brandon J. Rees, Acting Director, Office of Investment, AFL-CIO, Feb. 3, 2014
AFR:	Letter from Americans for Financial Reform, March 5, 2014
Ahmad:	Letter from Mohamed Ahmad, Aug. 21, 2014
AICPA:	Letter from The American Institute of Certified Public Accountants, Feb. 3, 2014
Amram 1:	Letter from Elan Amram, Feb. 3, 2014
Amram 2:	Letter from Elan Amram, Feb. 3, 2014
Angel 1:	Letter from James J. Angel, Ph.D., CFA, Visiting Associate Professor, Georgetown University, Feb. 5, 2014
Angel 2:	Letter from James J. Angel, Ph.D., CFA, Visiting Associate Professor, Georgetown University, Jul. 1, 2014

AngelList:	Letter from Naval Ravikant, CEO, AngelList, Jan. 24, 3014
Anonymous 1:	Letter from an anonymous person, Nov. 9, 2013
Anonymous 2:	Letter from an anonymous person, Nov. 13, 2013
Anonymous 3:	Letter from an anonymous person, Nov. 25, 2013
Anonymous 4:	Letter from an anonymous person, Dec. 5, 2013
Anonymous 5:	Letter from an anonymous person, Jan. 25, 2014
Anonymous 6:	Letter from an anonymous person, Feb. 7, 2014
Arctic Island 1:	Letter from Scott Purcell, Founder and CEO, Arctic Island LLC, Nov. 4, 2013
Arctic Island 2:	Letter from Scott Purcell, Founder and CEO, Arctic Island LLC, Dec. 4, 2013
Arctic Island 3:	Letter from Scott Purcell, Founder and CEO, Arctic Island LLC, Dec. 4, 2013
Arctic Island 4:	Letter from Scott Purcell, Founder and CEO, Arctic Island LLC, Dec. 4, 2013
Arctic Island 5:	Letter from Scott Purcell, Founder and CEO, Arctic Island LLC, Dec. 6, 2013
Arctic Island 6:	Letter from Scott Purcell, Founder and CEO, Arctic Island LLC, Dec. 6, 2013
Arctic Island 7:	Letter from Scott Purcell, Founder and CEO, Arctic Island LLC, Dec. 6, 2013
Arctic Island 8:	Letter from Scott Purcell, Founder and CEO, Arctic Island LLC, Dec. 31, 2013
ASSOB:	Letter from Paul M. Niederer, CEO, ASSOB Equity Funding Platform Australia, Oct. 25, 2013
ASTTC:	Letter from Mark C. Healy, President and Chief Executive Officer, American Stock Transfer & Trust Company, Brooklyn, New York, Feb. 3, 2014
AWBC:	Letter from Marsha Bailey, Chair, Association of Women's Business Centers, Feb. 3, 2014

BackTrack:	Letter from Randy Shain, Founder and EVP, BackTrack Reports, Nov. 12, 2013
Ball:	Letter from Robert Ball, Feb. 1, 2014
BCFCU:	Letter from Margot Brandenburg, Chair, Brooklyn Cooperative Federal Credit Union, New York, New York, Feb. 3, 2014
Benavente:	Letter from Javier E. Benavente, Jan. 16, 2014
Benjamin:	Letter from Jordan Benjamin, Nov. 30, 2013
BetterInvesting:	Letter from Kamie Zaracki, Chief Executive Officer, et. al., Jul. 29, 2014
Borrell:	Letter from Monica L. Borell, Jan. 27, 2014
Brown D.:	Letter from Douglas Brown, Start-up business owner, Jan. 29, 2014
Brown J.:	Letter from J. Robert Brown, Jr., Professor of Law, University of Denver, Sturm College of Law, Jan. 27, 2014
Bullock:	Letter from Leo M. Bullock, IV, Nov. 10, 2013
Bushroe:	Letter from Fred Bushroe, Oct. 29, 2013
CalTech Entrepreneurs:	Letter from Russell M. Frandsen, Esquire, The Business Legal Group Executive Committee of the Caltech Entrepreneurs Forum, Jan. 29, 2014
Campbell R.:	Letter from Rutheford B. Campbell, Jr., Spears-Gilbert Professor of Law, University of Kentucky, Feb. 14, 2014
CAMEO:	Letter from Claudia Viek, CEO, California Association for Micro Enterprise Opportunity, Feb. 3, 2014
CapSchedule:	Letter from Scott Purcell, CapSchedule.com, LLC, Oct. 23, 2013
CarbonTech:	Letter from Robert Shatz, CEO, CarbonTech Global LLC, Oct. 24, 2013
CCI:	Letter from Carrie Devorah, The Center For Copyright Integrity, Feb. 3, 2014

CEI:	Letter from John Berlau, Senior Fellow, Finance and Access to Capital, Competitive Enterprise Institute, Feb. 3, 2014
CFA Institute:	Letter from Kurt N. Schacht, CFA, Managing Director, Standards and Financial Market Integrity, and Linda L. Rittenhouse, Director, Capital Markets, CFA Institute, Feb. 3, 2014
CFIRA 1:	Letter from Freeman White, Board Member, et al., CFIRA, Jan. 19, 2014
CFIRA 2:	Letter from Kim Wales, Executive Board Member, and Chris Tyrrell, Chairman, CFIRA, Jan. 20, 2014
CFIRA 3:	Letter from Kim Wales, Executive Board Member, and Chris Tyrrell, Chairman, CFIRA, Jan. 26, 2014
CFIRA 4:	Letter from Kim Wales, Executive Board Member, et al., CFIRA, Jan. 26, 2014
CFIRA 5:	Letter from Kim Wales, Founder and CEO, Wales Capital, and Executive Board Member, CFIRA, Jan. 26, 2014
CFIRA 6:	Letter from Joy Schoffler, Board Member, et al., CFIRA, Jan. 27, 2014
CFIRA 7:	Letter from Mary Juetten, Board Member, et al., CFIRA, Jan. 31, 2014
CFIRA 8:	Letter from Jonathan Miller, Board Member, et al., CFIRA
CFIRA 9:	Letter from Daryl Bryant, Board Member, et al., CFIRA, Feb. 4, 2014
CFIRA 10:	Letter from Robert Carbone, CFIRA Board Member, CrowdBouncer, CEO, New York, New York, Feb. 6, 2014
CFIRA 11:	Letter from Chris Tyrell, Chairman, and Kim Wales, Executive Board Member, CFIRA, New York, New York, Feb. 6, 2014
CFIRA 12:	Letter from Kim Wales, CEO, Wales Capital, and CFIRA Executive Board Member, and Scott

	Purcell, CEO, Artic Island, and CFIRA Board Member, Apr. 24, 2014
City First:	Letter from John Hamilton, President, City First Enterprises, Washington, District of Columbia, Feb. 3, 2014
Clapman:	Letter from Mordechai Clapman, Oct. 25, 2013
ClearTrust:	Letter from Kara Kennedy, Executive Director, ClearTrust, LLC, Jan. 20, 2014
Cole A.:	Letter from Adam Cole, Nov. 24, 2013
Cole D.:	Letter from Don Cole, Oct. 25, 2013
Commonwealth of Massachusetts:	Letter from William F. Galvin, Secretary of the Commonwealth of Massachusetts, Feb. 3, 2014
Computershare:	Letter from Martin (Jay) J. McHale, Jr., President, US Equity Services, Computershare, Canton, Massachusetts, Feb. 3, 2014
Concerned Capital:	Letter from Bruce Dobb, Concerned Capital - A Social Benefit Corp., Feb. 2, 2014
Consumer Federation:	Letter from Barbara Roper, Director of Investor Protection, Consumer Federation of America, Feb. 2, 2014
Craw:	Letter from Kristopher R. Craw, J.D., Denver, Colorado, Jun. 14, 2014
CSTTC:	Letter from Steven G. Nelson, President and Chairman of Continental Stock Transfer Trust Company, Jan. 31, 2014
CST:	Letter from Carylyn K. Bell, President, Corporate Stock Transfer, Inc., Jan. 15, 2014
Coombs:	Letter from Jason Coombs, Feb. 7, 2014
CfPA:	Letter from Charles Sidman, MBA, PhD, President and Chair, for the Board of, the Crowdfunding Professional Association, Feb. 3, 2014
CRF:	Letter from Frank Altman, President and CEO, Community Reinvestment Fund, USA, Feb. 3, 2014

Cromwell:	Letter from David M. Cromwell, Yale School of Management, Adjunct Professor of Entrepreneurship, Oct. 27, 2013
CrowdBouncer:	Letter from Robert C. Carbone, Founder & CEO, CrowdBouncer, Inc., Buffalo, New York, Feb. 3, 2014
CrowdCheck 1:	Letter from Sara Hanks, CEO, CrowdCheck, Inc., Jan. 9, 2014
CrowdCheck 2:	Letter from Andrew D. Stephenson, Research Manager, CrowdCheck, Inc., Jan. 23, 2014
CrowdCheck 3:	Letter from Sara Hanks, CEO, CrowdCheck, Inc., Feb. 2, 2014
CrowdCheck 4:	Letter from Brian R. Knight, VP, CrowdCheck, Inc., Feb. 2, 2014
CrowdFundConnect:	Letter from Randy A. Shipley, CrowdFundConnect Incorporated, Dec. 14, 2013
Crowdpassage 1:	Letter from Matthew R. Nutting, Esq., Executive Director, National Legal Director, Crowdpassage.com, Jan. 31, 2014
Crowdpassage 2:	Letter from Matthew R. Nutting, Esq., Executive Director, National Legal Director, Crowdpassage.com, Jan. 31, 2014
Crowdpassage 3:	Letter from Matthew R. Nutting, Esq., Executive Director, National Legal Director, Crowdpassage.com, Jan. 31, 2014
CrowdStockz:	Letter from Frederic C. Schultz, Esq. and Alastair Onglingswan, Esq., Owners of CrowdStockz.com., CrowdStockETFs.com., and CrowdStockFunds.com, Feb. 3, 2014
Crowley:	Letter from Vincent Crowley, Nov. 11, 2013
CrwdCorp:	Letter from Sean Shepherd, Founder & Chief Executive Officer, CrwdCorp, LLC, Jan. 16, 2014
Cunningham 1:	Letter from William Michael Cunningham, Social Investing Advisor, Washington, District of Columbia, Feb. 3, 2014

Cunningham 2:	Letter from William Michael Cunningham, M.B.A., M.A., Social Investing Advisor, Washington, District of Columbia, Feb. 3, 2014
dbb*mckennon:*	Letter from dbb*mckennon*, Certified Public Accountants, Oct. 1, 2014
DeMarco:	Letter from Peter J. DeMarco, Student, Stanford Law School, Nov. 12, 2013
Denlinger 1:	Letter from Craig Denlinger, CPA, Denver, Colorado, Feb. 3, 2014
Denlinger 2:	Letter from Craig Denlinger, CPA, CrowdfundCPA, Aug. 21, 2014
Doctor:	Letter from Roger Doctor, Dec. 10, 2013
Donohue:	Letter from Patrick E. Donohue, Minneapolis, Minnesota, Feb. 24, 2014
DreamFunded:	Letter from Manny Fernandez, Co-Founder and CEO, www.DreamFunded.com, Jan. 8, 2014
Duke:	Letter from Heather Duke, Dec. 3, 2013
EarlyShares:	Letter from Joanna Schwartz, CEO, EarlyShares.com, Inc., Feb. 3, 2014
Echterling:	Letter from Ian Echterling, Entrepreneur Feb. 21, 2014
Ellenbogen:	Letter from David M. Ellenbogen, Jan. 27, 2014
EMKF:	Letter from Alicia Robb, Ph.D, Senior Fellow, and Dane Stangler, Vice President, Research & Policy, Ewing Marion Kauffman Foundation, Feb. 3, 2014
Empire Stock:	Letter from Matthew J. Blevins, Vice President, Empire Stock Transfer Inc., Jan. 15, 2014
EquityNet:	Letter from Judd E. Hollas, Founder and CEO, EquityNet, LLC
Equity Stock:	Letter from Mohit Bhansali, Chief Operating Officer, Equity Stock Transfer LLC, New York, New York, Feb. 3, 2014

Ex24:	Letter from James. P. Lennane, ex24, Inc., Jan. 29, 2014
EY:	Letter from Ernst & Young LLP, Feb. 3, 2014
Farnkoff:	Letter from Brian Farnkoff, Editor-in-Chief, Journal of Contemporary Health Law and Policy, Feb. 3, 2014
Farese:	Letter from Robert L. Farese, Jr., Oct. 30, 2014
FAST:	Letter from Salli A. Marinov, President and CEO, First American Stock Transfer, Inc., January 23, 2014
Feinstein:	Letter from Todd Feinstein, Feinstein Law, P.A., Feb. 3, 2014
Finkelstein:	Letter from Elizabeth R. Makris, Finkelstein Thompson LLP, Jan. 31, 2014
FOLIOfn:	Letter from Michael J. Hogan, President & Chief Executive Officer, FOLIOfn Investments, Inc., McLean, Virginia, Feb. 3, 2014
Frutkin:	Letter from Jonathan Frutkin, The Frutkin Law Firm, Jan. 30, 2014
Fryer:	Letter from Gregory S. Fryer, Esq., Partner, Verrill Dana, LLP, Portland, Maine, Feb. 5, 2014
FSI:	Letter from David T. Bellaire, Esq., Executive Vice President & General Counsel, Financial Services Institute, Feb. 3, 2014
Fund Democracy:	Letter from Mercer Bullard, President and Founder, Fund Democracy, Associate Professor, University of Mississippi School of Law, Oxford, Mississippi, Feb. 3, 2014
Funderbuddies:	Letter from John Mark Wendler, CPA, Funderbuddies, Nov. 26, 2013
FundHub 1:	Letter from Kendall Almerico, Crowdfunding Expert, Attorney and CEO, Fund Hub and ClickStartMe, Jan. 29, 2014

FundHub 2:	Letter from Kendall Almerico, Crowdfunding Attorney and CEO of FundHub.Biz, Tampa, Florida, Oct. 8, 2014
Generation Enterprise:	Letter from Ubon Isang, Executive, Generation Enterprise Corporation, Oct. 24, 2013
Gibb:	Letter from Jeremy Gibb, Nov. 13, 2013
Gill:	Letter from Michael D. Gill, III, Esq., Jan. 22, 2014
Gimpelson 1:	Letter from Alexander Gimpelson, Chest Nut Hill, Massachusetts, Feb. 3, 2014
Gimpelson 2:	Letter from Alexander Gimpelson, Chest Nut Hill, Massachusetts, Feb. 3, 2014
Grassi:	Letter from Louis C. Grassi, CPA, CFE, Managing Partner, Grassi and Co., Jan. 20, 2014
Graves:	Letter from Sam Graves, Chairman, U.S. House of Representatives, Committee on Small Business, Washington, District of Columbia, Feb. 3, 2014
Greenfield:	Letter from Richard D. Greenfield, Esq., Greenfield Goodman LLC, Nov. 10, 2013
Greer:	Letter from Diana Greer, Jan. 27, 2014
Growthfountain:	Letter from Growthfountain LLC, Jan. 7, 2014
GSJ Advisors:	Letter from George Surgeon, President and CEO, GSJ Advisors, Ltd., Feb. 3, 2014
Guzik 1:	Letter from Samuel S. Guzik, Guzik and Associates, Los Angeles, California, Feb. 11, 2014
Guzik 2:	Letter from Samuel S. Guzik, Guzik and Associates, Los Angeles, Feb. 20, 2014
Guzik 3:	Letter from Samuel S. Guzik, Guzik and Associates, Los Angeles, California, Feb. 28, 2014
Hackers/Founders:	Letter from Charles Belle, Ken Priore, and Timothy Yim, Hackers/Founders, Feb. 3, 2014
Hakanson:	Letter from Sten E. Hakanson, Stillwater, Minnesota, Feb. 28, 2014

Hamilton:	Letter from Brenda L. Hamilton, Hamilton & Associates Law Group, P.A., Nov. 8, 2013
Hamman:	Letter from Charles J. Hamman, Oct. 24, 2013
Harrison:	Letter from Mark Harrison, Ph.D., Jan. 6, 2014
Holland:	Letter from Alexandra D. Holland, Ph.D., Founder and CEO, PIARCS, PBC, June 3, 2014
Martin:	Letter from Andrew Martin, OFS, CB, Rockville, Maryland, Oct. 18, 2014
MCS:	Letter from Andrew M. Hartnett, Missouri Commissioner of Securities, Feb. 3, 2014
Merkley:	Letter from Jeffrey A. Merkley, United States Senator, Apr. 29, 2014
Haylock:	Letter from Todd Haylock, Dec. 10, 2013
Heritage:	Letter from David R. Burton, Senior Fellow in Economic Policy, The Heritage Foundation, Feb. 3, 2014
Hyatt:	Letter from Todd R. Hyatt, Nov. 6, 2013
IAC Recommendation:	Recommendation of the SEC's Investor Advisory Committee: Crowdfunding Regulations, Apr. 10, 2014
iCrowd:	Letter from J. Bradford McGee and John P. Callaghan, Founders, iCrwod, LLC, Jan. 31, 2014
Inkshares:	Letter from Adam J. Gomolin, General Counsel, Inkshares, Inc., Feb. 3, 2014
Jacobson:	Letter from William A. Jacobson, Clinical Professor of Law, Cornell Law School, and Director, Cornell Securities Law Clinic, Ithaca, New York, Feb. 3, 2014
Jazz:	Letter from Jim C. Shaw, Jazz Gas, Jan. 12, 2014
Johnston:	Letter from Phil Johnston, Feb. 3, 2014
Joinvestor:	Letter from Bryan Healey, CEO, Joinvestor, Jan. 2, 2014

Kelso:	Letter from Carl Kelso, Jan. 7, 2014
Kickstarter Coaching:	Letter from Jay Wittner, President Kickstarter Coaching, Bradenton, Florida, Feb. 3, 2014
Kingonomics:	Letter from Rodney S. Sampson, CEO, Kingonomics, Feb. 3, 2014
Kishon:	Letter from Mannis Kishon, Dec. 22, 2013
Knudsen:	Letter from Michael Knudsen, Jan. 6, 2014
Konecek:	Letter from Kathleen Konecek, Nov. 30, 2013
Langrell:	Letter from Alex M. Langrell, Camp Pendelton, California, Jan. 21, 2014
Leverage PR:	Letter from Joy Schoffler, Principal, Leverage PR, Austin, Texas, Sep. 2, 2014
Lopossa:	Letter from Gabriel M. Lopossa, Oct. 30, 2013
Luster:	Letter from Louise Luster, Oct. 31, 2013
Mahoney:	Letter from Steve Mahoney, Managing Director, Highlands Ranch, Colorado, Jan. 20, 2014
Mantel:	Letter from Russ Mantel, Oct. 23, 2013
M.A.V.:	Letter from M.A.V., Nov. 3, 2013
Marsala:	Letter from Charles E. Marsala -Profitibale Dining LLC, Feb. 15, 2014
McCulley:	Letter from Matthew McCulley, Jan. 10, 2014
McGladrey:	Letter from McGladrey LLP, Feb. 3, 2014
Meling:	Letter from Rosemary Meling, Oct. 30, 2013
Menlo Park:	Letter from James O. Mason, Founder/CEO, Menlo Park Social Media Crowdfunding Incubator, Feb. 28, 2014
Miami Nation:	Letter from Ben Barnes, Director of Tribal Gaming, Miami Nation Enterprises, Oct. 25, 2013
Milken Institute:	Letter from Daniel S. Gorfine, Director, Financial Markets Policy, and Staci Warden, Executive

	Director, Center for Financial Markets, Milken Institute, Washington, District of Columbia, Feb. 3, 2014
Mlinarich:	Letter from Brett A. Mlinarich, Jan. 2, 2014
Mollick:	Letter from Ethan R. Mollick, Edward B. and Shirley R. Shils Assistant Professor of Management, Wharton School, University of Pennsylvania, Phildelphia, Pennsylvania, Feb. 5, 2014
Morse:	Letter from Matt R. Morse, Sr., Dec. 3, 2013
Moskowitz:	Letter from Yonatan Moskowitz, Nov. 13, 2013
Moyer:	Letter from Mike Moyer, Adjunct Associate Professor of Entrepreneurship at the University of Chicago Booth School of Business, Adjunct Lecturer of Entrepreneurship at Northwestern University, Jan. 25, 2014
Mountain Hardwear:	Letter from Alan A. Tabor, Co-founder, Mountain Hardwear, Jan. 27, 2014
Multistate Tax:	Letter from Frank L. Dantonio, Managing Principal, Multistate Tax Service, LLC, Oct. 29, 2013
NAAC:	Letter from Faith Bautista, President and CEO, National Asian American Coalition, Oct. 31, 2013
NACVA:	Letter from David M. Freedman, Editorial Advisor, The Value Examiner magazine (NACVA), Jan. 16, 2014
NAHB:	Letter from David L. Ledford, Senior Vice President, Housing Finance & Regulatory Affairs, National Association of Home Builders, Jan. 31, 2014
NASAA:	Letter from Andrea Seidt, President, North American Securities Administrators Association, Inc. (NASAA)
NASE:	Letter from Katie Vlietstra, Vice President of Government Relations Public Affairs, The National Association for the Self-Employed, Washington, District of Columbia, Feb. 3, 2014

NaviGantt:	Letter from Christopher R. York, CEO, NaviGantt, Jan. 27, 2014
NYSSCPA:	Letter from J. Michael Kirkland, President, New York State Society of Certified Public Accountants, Jan. 20, 2014
Nether:	Letter from Darrell W. Nether, Nov. 1, 2013
NFIB:	Letter from Dan Danner, President and CEO, National Federation of Independent Business, Feb. 3, 2014
NPCM:	Letter from Robert C. Guinto, Jr., President, Non Profit Capital management, LLC, Oct. 24, 2013
NSBA:	Letter from Todd O. McCracken, President, National Small Business Association, Feb. 3, 2014
Odhner:	Letter from Chad E. Odhner, Nov. 25, 2013
ODS:	Letter from Faye Morton, General Counsel, Oklahoma Department of Securities, Feb. 3, 2014
Omara:	Letter from Sherouk Omara, Nov. 14, 2013
Otherworld:	Letter from Mark Henry, Founder, Otherworld Pictures, Apr. 11, 2014
Parsont:	Letter from Jason W. Parsont, Feb. 18, 2014
Partners:	Letter from Jeannine Jacokes, CEO, Partners for the Common Good, Washington DC, District of Columbia, Feb. 3, 2014
Patel:	Letter from Raj Patel, Jan. 17, 2014
PBA:	Letter from Graham R. Laub, Chair, and Katayun I. Jaffari, Vice Chair, Securities Regulation Committee of the Business Law Section, Philadelphia Bar Association, Philadelphia, Pennsylvania, Feb. 3, 2014
Peers:	Letter from Kit Hayes, Campaign Director, Peers.org, Feb. 7, 2014
Perfect Circle:	Letter from Frederick C. Young, Perfect Circle Solutions, Oct. 30, 2013

PeoplePowerFund:	Letter from Steve Mayer, PeoplePowerFund.com, Jan. 31, 2014
Phillips:	Letter from Everette Phillips, Entrepreneur, Jan. 15, 2014
Pioneer Realty:	Letter from Charles E. Williams, MBA, EA, Founder and Managing Director, Pioneer Realty Capital, Jan 15, 2014
Platkin:	Letter from Matthew Platkin, Nov. 13, 2013
Powers:	Letter from Jordan Berg Powers, Nov. 4, 2013
PPA:	Letter from Douglas R. Slain, Managing Partner, Private Placement Advisors LLC
Projectheureka:	Letter from Anthony and Erika Endres, Projectheureka LLC, Nov. 17, 2013
Propellr 1:	Letter from Todd M. Lippiatt, CEO, Propellr, LLC, Jan. 27, 2014
Propellr 2:	Letter from Todd M. Lippiatt, CEO, Propellr, LLC, Jan. 27, 2014
Public Startup 1:	Letter from Jason Coombs, Co-Founder and CEO, Public Startup Company, Inc., Dec. 15, 2013
Public Startup 2:	Letter from Jason Coombs, Co-Founder and CEO, Public Startup Company, Inc., Feb. 3, 2014
Public Startup 3:	Letter from Jason Coombs, Co-Founder and CEO, Public Startup Company, Inc., Feb. 11, 2014
Public Startup 4:	Letter from Jason Coombs, Co-Founder and CEO, Public Startup Company, Inc., Feb. 22, 2014
Qizilbash:	Letter from Muhammad A. Qizilbash, Dec. 18. 2013
Raindance:	Letter from Jeffrey L. Tucker, CEO, The Raindance Group, Dec. 17, 2013
Ramsey:	Letter from Rebecca Ramsey, Oct. 24, 2013
Reed:	Letter from Terry Reed, J.D., Jan. 21, 2014
Reichman:	Letter from Vic Reichman, Esq., Dec. 2, 2013

RFPIA:	Letter from T. W. Kennedy, BE, CEO, Regulated Funding Portal Industry Association, Jan. 26, 2014
Ritter:	Letter from Justin A. Ritter, Esquire, Associate Attorney, Spinella, Owings & Shaia, P.C., Nov. 18, 2013
RoC:	Letter from Sang H. Lee, CEO, Return on Change, Jan. 30, 2014
RocketHub:	Letter from Alon Hillel-Tuch and Jed Cohen, RocketHub, New York, New York, Feb. 3, 2014
Rosenthal O.:	Letter from Oren Rosenthal, Attorney, Nov. 4, 2013
Sam H.:	Letter from Sam H., Oct. 27, 2013
Sander:	Letter from Steven M. Sander, CEO, Oct. 27, 2013
Sarles:	Letter from Jeff Sarles, Oct. 25, 2013
Saunders:	Letter from R. Kevin Saunders, Staff Editor, Vanderbilt Journal of Entertainment Technology Law, Nashville, Tennessee, Feb. 3, 2014
Sawhney:	Letter from Sanjay Sawhney, Jan. 27, 2014
SBA Office of Advocacy:	Letter from Winslow Sargeant, Ph.D., Chief Counsel for Advocacy, and Dillon Taylor, Assistant Chief Counsel for Advocacy, SBA Office of Advocacy, Jan. 16, 2014
SBEC:	Letter from Karen Kerrigan, President & CEO, Small Business & Entrepreneurship Council, Feb. 3, 2014
SBM:	Letter from Cassie Mills, Communications Associate, Small Business Majority, Feb. 4, 2014
Schatz:	Letter from Jonathan Schatz, Nov. 13, 2013
Schwartz:	Letter from Andrew A. Schwartz, Associate Professor of Law, University of Colorado, Boulder, Colorado, Feb. 3, 2014
Scruggs:	Letter from Frank Scruggs, Jan. 17, 2014
SeedInvest 1:	Letter from Kiran Lingam, Esq., General Counsel, SeedInvest, Jan. 21, 2014

SeedInvest 2:	Letter from Kiran Lingam, General Counsel, SeenInvest, Jan. 22, 2014
SeedInvest 3:	Letter from Kiran Lingam, Esq., General Counsel, SeedInvest, Feb. 3, 2014
Seed&Spark:	Letter from Max Silverman, COO, Seed & Spark
Sewell:	Letter from Michael J. Sewell, Esq., Jan 17, 2014
Seyfarth:	Letter from Seyfarth Shaw LLP, New York, New York, Feb. 10, 2014
SFAA:	Letter from Robert. J. Duke, Corporate Counsel, The Surety & Fidelity Association of America, Nov. 19, 2013
Sfinarolakis	Letter from Manolis E. Sfinarolakis, CFIRA, CFPA, NLCFA, New Britain, Connecticut, Aug. 6, 2014
Sharewave:	Letter from Joshua S. Levine, Co-Founder and CEO, Sharewave, LLC, Dec. 18, 2013
Smith D.:	Letter from Darrell Smith, Jan. 19, 2014
Smith K.:	Letter from Kevin G. Smith, Electrical Engineer, Oct. 31, 2013
Song:	Letter from Ntxhi Song, Student, Johnson and Wales University Charlotte, Charlotte, North Carolina, Feb. 3, 2014
STA:	Letter from Charles V. Rossi, Chairman, STA Board Advisory Committee, The Securities Transfer Association, Inc., Dec. 18, 2013
Stalt:	Letter from Bill Senner, Stalt, Inc., Jan. 27, 2014
StartEngine 1:	Letter from Ron Miller, CEO, StartEngine, Los Angeles, California, Jul. 25, 2014
StartEngine 2:	Letter from Ron Miller, CEO, StartEngine Crowdfunding, Inc., Oct. 7, 2014
StartupValley:	Letter from Daryl H. Bryant, CEO, StartupValley, Inc., Jan. 15, 2014

Stephenson:	Letter from Andrew D. Stephenson, Brian Knight, and Matthew Bahleda, Feb. 3, 2014
Stieglitz:	Letter from Edward B. Stieglitz, Oct. 28, 2013
Syed:	Letter from Idrus R. Syed, MBA, Oct. 24, 2013
Tafara:	Letter from Peter Tafara, Nov. 8, 2013
Hillside:	Letter from Anthony M. Tate, Hillside Technological Innovation LLC, Cedar Rapids, Iowa, Feb. 11, 2014
TAN:	Letter from Olawale Ayeni, MBA, and Bolaji Olutade, Ph.D., The African Network, Dec. 12, 2013
Taylor M.:	Letter from Mack Taylor, Nov. 8, 2013
Taylor R.:	Letter from Ryan S. Taylor, Crowdfunder, Oct. 24, 2013
Taylor T.:	Letter from Terry L. Taylor, Oct. 24, 2013
Thomas 1:	Letter from Jeff Thomas, JD, CPA, Chair of Business and Associate Professor, Johnson & Wales University, Charlotte, North Carolina, Feb. 3, 2014
Thomas 2:	Letter from Jeff Thomas, JD, CPA, Chair of Business and Associate Professor, Charlotte, North Carolina, Feb. 3, 2014
Thompson:	Letter from Lyle Thompson, Entrepreneur, Dec.10, 2013
Tiny Cat:	Letter from L. David Varvel and Ellenor Varvel, Founders, Tiny Cat Loans, Feb. 3, 2014
TraceFind:	Letter from Wendi C. Hawley, MA, ATR-BC, CEO, TraceFind Technologies, Inc., Oct. 24, 2013
Traklight:	Letter from Mary E. Juetten, Founder & CEO, Traklight.com, Feb. 2, 2014
Tucker:	Letter from Gary Tucker, Feb. 17, 2014
US Black Chambers:	Letter from Ron Busby, President, US Black Chambers, Inc., Washington, District of Columbia, Feb. 3, 2014

U.S. Chamber of Commerce:	Letter from Tom Quaadman, Vice President, Center for Capital Markets Competitiveness, U.S. Chamber of Commerce, Feb. 3, 2014
Verinvest:	Letter from David Benway, Chief Executive Officer, Verinvest Corporation, Jan. 17, 2014
Vann:	Letter from James Vann, Greenfield, Missouri, Apr. 11, 2014
Vest:	Letter from Sean Osterday & Peter Wild, Vest Inc., San Francisco, California, Feb. 3, 2014
Vidal:	Letter from Eduardo Vidal, Jan. 27, 2014
Vossberg:	Letter from Trevor Vossberg, Oct. 23, 2013
Wales Capital 1:	Letter from Kim Wales, Founder and CEO, Wales Capital, Feb. 3, 2014
Wales Capital 2:	Letter from Kim Wales, Founder and CEO, Wales Capital, Mar. 2, 2014
Wales Capital 3:	Letter from Kim Wales, Founder and CEO, Wales Capital, Mar. 12, 2014
WealthForge:	Letter from Mathew Dellorso, CEO, WealthForge Holdings, Inc., Richmond, Virginia, Feb. 3, 2014
Wear:	Letter from Zak Wear, Dec. 10, 2013
Wefunder:	Letter from Nicholas Tommarello, CEO, Wefunder, January 31, 2014
Whitaker Chalk:	Letter from John R. Fahy and Wayne M. Whitaker, Whitaker Chalk Swindle & Schwartz PLLC, Jan. 7, 2014
Wilhelm:	Letter from Jonathan R. Wilhelm, Jan. 27, 2014
Wilson:	Letter from Margaret A. Wilson, Professor of Technology Commercialization, Austin, Texas, Feb. 3, 2014
Winters:	Letter from Dennis Winters, Esq., Jan. 9, 2014
WIPP:	Letter from Barbara Kasoff, President, Women Impacting Public Policy, Feb. 3, 2014

Woods:	Letter from Thell M. Woods, Jan. 13, 2014
Yudek:	Letter from David B. Kopp, CEO, Yudek, Inc. Oct. 29, 2013
Zeman:	Letter from Jason Zeman, Nov. 30, 2013
Zhang:	Letter from Runan Zhang, Esq., Law Offices of Runan Zhang, Washington, District of Columbia, Feb. 3, 2014
7thenterprise:	Letter from Jarone V. Price, CEO, 7thenterprise International Inc., Jan. 22, 2014
11 Wells:	Letter from Robert McManus, The 11 Wells Spirits Company, Jan. 28, 2014