# Request for Reconsideration of the Audit Requirement for Capital Raised by CrowdFunding for Businesses Raising $500,000 or More

Ladies and Gentlemen,

I am greatly concerned that the audit requirements for businesses seeking to raise more than $500,000 may be too burdensome to be serviceable to early-startup businesses or investors. The SEC should consider that some regulations, like the above, are particularly burdensome when examined in light of the regulations of the United Kingdom, which already has CrowdFunding for equity provisions adopted into its legal structure—and provides tax relief for investors under its Enterprise Investment Scheme.

(http://en.wikipedia.org/wiki/Enterprise_Investment_Scheme)

While it is understood that the role of the SEC is to protect individuals and the financial system from systemic fraud and abuse some of the regulations which have been currently proposed are unduly burdensome. The remedy should never be worse than the disease. This is particularly relevant in consideration of the requirement that financial statements be audited for firms raising $500,000 or more.

(http://www.forbes.com/sites/tanyaprive/2012/11/06/inside-the-jobs-act-equity-crowdfunding-2/)

Consider that the average cost for such an audit of a small organization is between $15,000 – 75,000 (http://www.entrepreneur.com/article/222806). The cost of performing this audit represents a total of between 1.5 - 15% of the total funds raised, averaging somewhere around 7% of total funds raised. While this expense may seem incidental to regulators and individuals who are used to reviewing large sums of money at banks and other multi-billion dollar institution, such an expense could very well starve a small organization in its early stages of money that is otherwise needed for payroll and operational expenses that are tied to directly creating value in the business. Indeed, 7% in this case may represent the entire salary of an individual working in the organization or the difference between investing in equipment and services which will make the company successful or not.

Such expenses create little economic value for the businesses raising capital (under further investigation) for the investors putting forward the funds. While it is acknowledged that audits do intend to create value for investors by allowing them to place greater reliance on the audited results. The unintended effect is that investors are unlikely to receive benefit from such requirements.

The reasons are thus:

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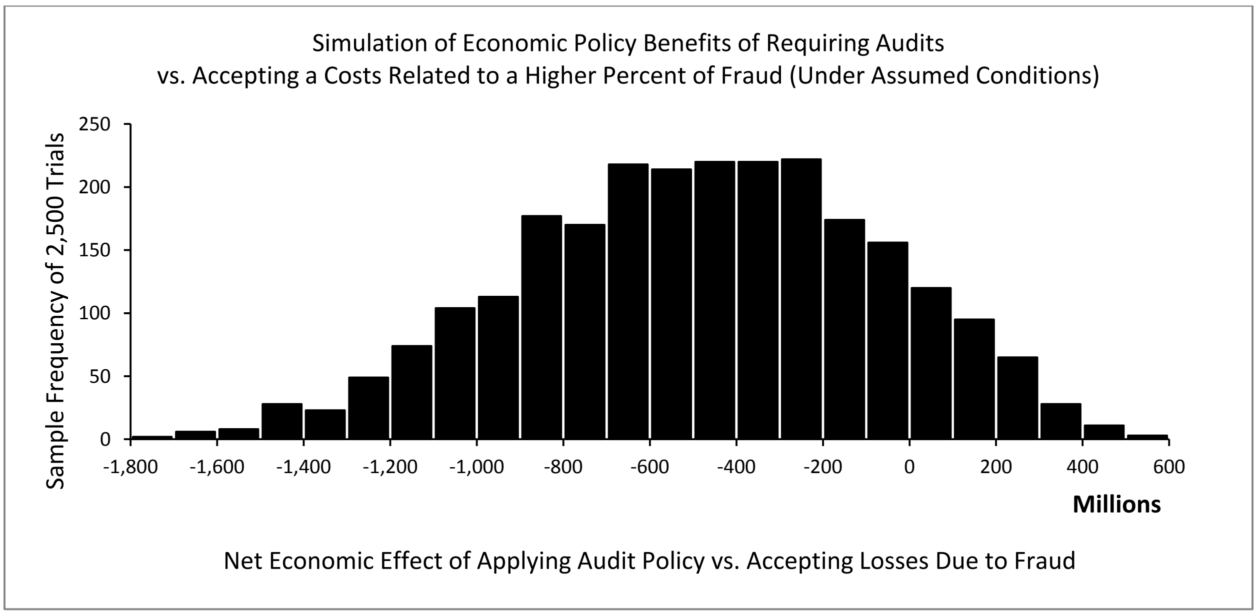
1. The audit requirement only reduces one kind of risk (fraud) in exchange for increasing other kinds of risk (business failure or forgone business startup).
2. Economically speaking, the degree of fraudulent activity which *might* occur is offset by the cost which certainly *must* occur.

Consequently a cost/benefit analysis (provided) should have been performed prior to recommending the policy. This analysis should have compared the decrease in *possible* fraud which application of the audit policy recommends against the decrease in *possible* business success/formation which is caused by the substantial cost of applying the audit's cost to all firms seeking to raise between $500,000 and 1,000,000.

I have done such a comparison and have provided the results for ready examination. What is apparent in the results of the analysis is that the cost of the policy recommendation is likely to overwhelm the benefits associated with it. Consequently, this policy should be considered a*egrescit medendo* (a cure worse than the disease).




(Graph 1: Summary of Simulation of 10,000 Cases—analysis below)

In light of the above, I recommend, at minimum, that the SEC defer such a requirement until further study can determine whether it is economically beneficial to the investment community. Because such provisions can always be added after the fact, if they are demonstrated to be economically beneficial, they should be deferred until such time as the study has yielded these results. Because time is of the essence in implementing these crowdfunding provisions, so that the US economy may continue its recovery and better compete with economies across the world, I recommend that this requirement for auditing be staid for the present time.

This issue is particularly relevant to me as I am currently looking to raise funds for a business venture which is designed to allow employers to find good employees more easily. This service is greatly needed in our current economic environment, and yet the provisions which the SEC would adopt related to CrowdFunding provisions contained in the JOBS Act unduly burden entrepreneurs and investors like myself who are merely trying to create good in the world without demonstrating that these provisions actually benefit either the marketplace or the businesses and investors that those markets are designed to serve.

I greatly appreciate the SEC's thoughtful consideration on this matter.

Sincerely,

Erin C. DeSpain
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# Analysis Of Aggregate Economic Impact of Implementing the Audit Requirement for 10,000 Cases

| SCENARIO 1: (DOES NOT INCLUDE AUDIT REQUIREMENT) | |
|---|---|
| Business Formation Without Audit Policy | 10,000 |
| Fraud Rate Without Audit Policy | 15.00% |
| Gross Economic Activity Without Audit Policy | 7,500,000,000 |
| Minus Cost of Fraudulent Activity Without Audit Policy | 1,125,000,000 |
| Minus Aggregate Cost of All Audits | - |
| **Net Gain Economic Gain Without Audit Policy** | **6,375,000,000** |
| **BETTER THAN ALTERNATIVE** | **525,937,500** |

| SCENARIO 2: (INCLUDES AUDIT REQUIREMENT) | |
|---|---|
| Business Formation With Audit Policy | 8,500 |
| Fraud Rate With Audit Policy | 2.25% |
| Gross Economic Value Created With Audit Policy | 6,375,000,000 |
| Minus Cost of Fraudulent Activity | 143,437,500 |
| Minus Aggregate Cost of All Audits | 382,500,000 |
| **Net Gain Economic Gain Of With Audit Policy** | **5,849,062,500** |
| **WORSE THAN ALTERNATIVE** | **(525,937,500)** |

| | |
|---|---|
| **ASSUMED CONSTANTS** | |
| 750,000 | Average Capital Raised By Business |
| 45,000 | Average Audit Cost |
| 15.00% | Fraud Rate |
| **SIMULATED VARIABLE INPUTS** | |
| 8.50% | Percent Reduction of Business Formation Due to Audit Policy (Low: 0%, Mean: 8.5%, High: 25%) |
| 85.00% | Percent Reduction of Fraudulent Activity Due to Audit Policy (Low: 0%, Average: 85%, High: 100%) |